IN THE

Supreme Court of the United States

OCTOBER TERM, 1976

No. 75-706

ADOLPH COORS COMPANY,

Petitioners,

VS.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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OPINIONS BELOW

First Case. The Opinion of the Tax Court in the first case is unreported, T. C. Memo. 1968-256, filed November 7, 1968 (Appendix A, pp. 1a-27a, infra); Commissioner's computation statement was filed with the Tax Court in the first case, after its above Opinion (Appendix B, pp. 28a-41a, infra); the Decision of the Tax Court in the first case was entered January 23, 1969 (Appendix C, pp. 42a-43a, infra).

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[1]Adolph Coors Company is referred to as Coors and Commissioner of Internal Revenue as Commissioner.

Second Instant Case. The Opinion of the United States Tax Court in a consolidated case, was filed June 12, 1973 and is reported at 60 T. C. 368 (1973) (Appendix D, pp. 44a-114a, infra); and the Opinion of the United States Court of Appeals Tenth Circuit, in the instant Coors case, was filed July 22, 1975 (Appendix E, pp. 115a-121a, infra).

JURISDICTION

The jurisdiction of this Court is invoked under 28 U.S.C. Sec. 1254(1). Coors' Petition for Rehearing En Banc was denied by the Division of the United States Court of Appeals Tenth Circuit August 25, 1975 (Appendix F, p. 122a, infra). The petition for certiorari is due November 24, 1975.

QUESTIONS PRESENTED

Where in the first case the Commissioner, after trial, abandoned his overhead issue determination and the Tax Court entered judgment against the Commissioner and for Coors, does the Tenth Circuit Court of Appeals opinion holding that res judicata and collateral estoppel doesn't apply in the present second case on its premise "there was no judicial determination" of the overhead issue and it "was not judicially determined" in the first case conflict with (I) the federal taxing statute, (II) several Circuit Courts decisions, and (III) decisions of the United States Supreme Court.

STATUTES AND RULES INVOLVED

Internal Revenue Code (1954) Section 6214(a) (Appendix G, p. 123a, infra).

Rules of Practice and Procedure, United States Tax Court, Rule 123(d) appears in Appendix H, p. 123a, infra.

STATEMENT

The parties and the overhead issue were the same in the first case for the prior years 1962, 1963 and 1964 and in the

instant second case for the following years 1965 and 1966. In both cases the Commissioner had determined and capitalized as overhead (1) part of the reported depreciation on idle construction and repair equipment, and (2) estimated indirect costs for self-constructed capital assets. These annual capitalized amounts were substantial and were currently added to taxable income for each of the five years in the Commissioner's two separate notices of deficiency, the first one for years 1962-1964 and the second notice of deficiency for 1965 and 1966. The two trials involved the Commissioner's changing of Coors' long and continuous use of a full absorption method of cost accounting, extending over a fifty-year period with the Commissioner's tacit approval, and in each case substantially the same set of events, accounting documents and expert witnesses were used.

FIRST CASE

In the first case Coors filed its petition with the Tax Court, in which it assailed the Commissioner's determined construction overhead and capitalized depreciation issue for each of the years 1962, 1963 and 1964. There was a full and complete trial on the merits before Tax Court Judge Murdock. After trial, Coors timely filed its brief with the Tax Court, in which it set forth requested findings of fact, law and argument to support its request that the Tax Court redetermine the overhead and capitalized depreciation issue for Coors and against the Commissioner.

The Commissioner, in his brief filed with the Tax Court, declined to further pursue the defense of his capitalized construction overhead and equipment depreciation determination for each of the three years. Thereupon Judge Murdock's Tax Court Opinion found as facts the ultimate amounts of self-construction overhead and idle construction equipment depreciation determined and disallowed by the Commissioner and now abandoned by him as follows (Appendix A, p. 2a, infra):

"The Commissioner in his brief abandons the disallowances of deductions made in the deficiency notice of $405,567.07 for 1962, $560,942.25 for 1963 and $310,866.81 for 1964 representing corporation costs of construction overhead and maintenance and costs of engineering department overhead. He also abandons disallowances of $59,-009.60 for 1962, $95,931.71 for 1963 and $122,076.56 for 1964 representing depreciation on construction equipment of the corporation."

The Commissioner's Computation Statement, which was thereupon filed with the Tax Court, finds overpayments in income taxes of $16,434.02 for 1962, $121,571.00 for 1963 and $156,322.58 for 1964. (Appendix B, pp. 28a, 29a and 30a, infra).

The Commissioner's said Computation Statement also finds as facts the amounts reported by Coors as Other expenses and Depreciation expense for the years 1962, 1963 and 1964, which the Commissioner had capitalized and added to income in his notice of deficiency and which he now was decreasing income by such amounts as follows (Appendix B, p. 31a, infra):

	Taxable Years Ended		
Name	**December 31, 1962**	**December 31, 1963**	**December 31, 1964**
Adolph Coors Company			
(Decreases) In Income			
(a) Other expenses — overhead	$(405,567.07)	$(560,942.25)	$(310,866.81)
(b) Depreciation expense	$(62,912.18)	$(58,160.75)	$(27,635.66)

The Commissioner's "Explanation of Adjustments" (Appendix B, p. 32a, infra) were as follows:

"1962

(a) The Commissioner in his brief abandoned the disallowance as operating expenses of costs of construction overhead and maintenance in the amount of $373,218.74 and costs of engineering department overhead in the amount of $32,348.33. Accordingly, your taxable income is decreased in the amount of $405,567.07.

1963

(a) The Commissioner in his brief abandoned the disallowance as operating expenses of costs of construction overhead and maintenance in the amount of $506,562.04 and costs of engineering department overhead in the amount of $54,380.21. Accordingly, your taxable income is decreased in the amount of $560,942.25.

1964

(a) The Commissioner in his brief abandoned the disallowance as operating expenses of costs of construction overhead and maintenance in the amount of $241,115.48 and costs of engineering department overhead in the amount of $69,751.33. Accordingly, your taxable income is decreased in the amount of $310,866.81."

The Commissioner's said computation statement finds as facts the amounts of depreciation reported as expenses by Coors on idle repair and construction equipment, which were disallowed and added to income and determined in the notice of deficiency by the Commissioner to be non-deductible overhead costs, and the Commissioner's Explanation of Adjustments for the amounts now conceded by him for the years

1962, 1963 and 1964 as follows (Appendix B, pp. 33a and 34a, infra):

> **1962.** The Commissioner in his brief abandoned his notice of deficiency determined disallowance of depreciation on idle construction equipment and addition to income of the amount of $59,009.60, which sum he now concedes should be deducted from the Commissioner's previous determined taxable income.
>
> **1963.** The Commissioner in his brief abandoned his notice of deficiency determined disallowance of depreciation on idle construction equipment and addition to income of $95,931.74, which sum he now concedes should be deducted from the Commissioner's previous determined taxable income.
>
> **1964.** The Commissioner in his brief abandoned his notice of deficiency determined disallowance of depreciation on idle construction equipment and addition to income of $122,076.56, which sum he now concedes should be deducted from the Commissioner's previous determined taxable income.

The Tax Court Decision following the filing of the Commissioner's Computation Statement and Judge Murdock's Decision entered January 23, 1969, stated as follows (Appendix C, p. 42a, infra):

> "Pursuant to the opinion of the Court filed November 7, 1968, and incorporating herein the facts recited in the respondent's computation as the findings[2] of the Court, it is
>
> ORDERED and DECIDED: That there is an overpayment in income tax for the taxable year

[2]In conflict with the Opinion of the Tenth Circuit Court of Appeals (Appendix E, p. 118a, infra), actually there were "either mediate or ultimate" findings made by the Tax Court in its first case.

> 1962 in the amount of $16,434.02 . . . That there is an overpayment in income tax for the taxable year 1963 in the amount of $121,571.00 . . . That there is an overpayment in income tax for the taxable year 1964 in the amount of $156,322.58 . . ."

The Commissioner appealed the first case to the Tenth Circuit Court of Appeals but later withdrew his appeal.

SECOND CASE

In the instant second case the Commissioner made the same overhead deficiency determination for the following years 1965 and 1966, with the amounts necessarily varying. The Commissioner also made a companion adjustment under Section 481 of the Internal Revenue Code, which computation therefor caused him to again make his same original deficiency capitalized overhead determination for the first case years 1962, 1963 and 1964, in direct contradiction of the Tax Court first case Opinion, decision and judgment redetermining the overhead issue against the Commissioner and for Coors. The Commissioner could have made and determined the same comparable Section 481 IRC issue determination in the first case.

Coors again filed a petition in the instant second case with the Tax Court, in which it assailed the Commissioner's same overhead second determination for the two following years 1965-1966, requesting the application of the doctrine of res judicata and collateral estoppel. The Tax Court in an opinion by a single substitute judge, who did not participate in the trial, concluded "the doctrines of res judicata and collateral estoppel do not apply" because of the Commissioner's abandonment of the overhead issue in the first case. (Appendix D, p. 82a, infra). Coors' Motion requesting review by the full Tax Court was denied.

A three judge division of the United States Court of Appeals, Tenth Circuit, in an Opinion authored by the one judge who was absent from the oral arguments hearing, stated as follows (Appendix E, pp. 118a-119a, infra):

> "The overhead capitalization issue was, as taxpayer correctly contends, raised in the first case. However, no findings, either mediate or ultimate, were made with respect thereto, and there was no judicial determination of the issue. To obtain the protection afforded by the doctrine of collateral estoppel an issue must have been raised, litigated and actually adjudged on the merits in the first proceeding. Here, the overhead issue was raised, but because it was abandoned by the IRS, was not judicially determined. Under these circumstances collateral estoppel cannnot apply."[3]

REASONS FOR GRANTING THE WRIT

Where in the first case the Commissioner, after trial, abandoned his overhead issue determination and the Tax Court entered judgment against the Commissioner and for Coors, the Tenth Circuit Court's Opinion[4] that res judicata and collateral estoppel doesn't apply in the present second case on its premise there was "no judicial determination" of the overhead issue and it "was not judicially determined" by the Tax Court in the first case conflicts with (I) the federal taxing statute, (II) several United States Circuit Court of Appeals decisions, and (III) decisions of the United States Supreme Court.

[3]The cited precedents by the Tenth Circuit Court of Appeals of Trapp v. United States, 177 F.2d 1 (10th Cir. 1949), cert. den'd.; Jones v. United States, 466 F.2d 131, 133 (10th Cir. 1972), cert. den'd.; and CIR v. Sunnen, 333 U.S. 591 (1948) are not authority for its Opinion. In conflict these three cited cases all held that collateral estoppel applies and, we submit, are authority for Coors' claim that in the instant second case collateral estoppel applies.

[4]In the instant second case neither the Tax Court nor the Tenth Circuit Court of Appeals directly held that the opinion and Decision of Tax Court Judge Murdock in the first case was not a final judgment on the merits.

I

IN CONFLICT WITH THE OPINION OF THE TENTH CIRCUIT COURT OF APPEALS, THE OPINION AND DECISION OF THE TAX COURT IN THE FIRST CASE WAS A JUDICIAL REDETERMINATION AND A JUDGMENT ON THE MERITS OF THE OVERHEAD ISSUE AGAINST THE COMMISSIONER AND FOR COORS, FOR PURPOSES OF THE APPLICATION OF RES JUDICATA AND COLLATERAL ESTOPPEL IN THE INSTANT SECOND CASE.

In the first case the Commissioner in his deficiency determination capitalized as overhead (1) part of the reported depreciation on idle construction and repair equipment, and (2) capitalized as overhead estimated indirect costs for self-constructed capital assets. Coors assailed the Commissioner's overhead determinations and requested a redetermination against the Commissioner and for Coors in its petition filed in the United States Tax Court.

There was a full and complete trial between the parties on the merits of the overhead issue before Judge Murdock of the Tax Court. The Commissioner, after trial, on brief defaulted on his right and obligation to brief the overhead issue and declined to continue to pursue the defense of his overhead determination. The Commissioner in his brief stated that he now abandons the overhead issue.

Judge Murdock in his Opinion[5] stated:

[5]The Opinion of the Tenth Circuit Court of Appeals makes the following erroneous findings: "By abandoning these adjustments, the respondent does not concede one way or the other that Adolph Coors Company's accounting treatment for these items is correct. The respondent is merely abandoning any attempt to change Adolph Coors Company's treatment of these items for the taxable years 1962, 1963 and 1964." These "findings" of the Tenth Circuit Court are merely self-serving statements taken from Commissioner's first case Tax Court brief, they are non-evidentiary findings and are not findings of Judge Murdock in the first case.

"The Commissioner in his brief abandons the disallowances of deductions made in the deficiency notice of $405,567.07 for 1962, $560,942.25 for 1963 and $310,866.81 for 1964 representing corporation costs of construction overhead and maintenance and costs of engineering department overhead. He also abandons disallowances of $59,009.60 for 1962, $95,931.71 for 1963 and $122,076.56 for 1964 representing depreciation on construction equipment of the corporation."

Thereupon the Commissioner filed his Computation Statement with the Tax Court finding overpayments in income taxes of $16,434.02 for 1962, $121,571.00 for 1963 and $156,322.58 for 1964. The Commissioner's Computation Statement also finds as facts the amounts of expenses reported by Coors, which were disallowed and determined by the Commissioner to be non-deductible overhead costs and now abandoned by the Commissioner for the years 1962, 1963 and 1964 as follows:

Year	Construction amounts	Engineering amounts	Depreciation
1962	$373,218.74	$32,348.33	$ 59,009.60
1963	506,562.04	54,380.21	95,931.74
1964	241,115.48	69,751.33	122,076.56

Judge Murdock's Tax Court Decision, which followed, incorporated the facts recited in the Commissioner's Computation Statement as the findings of the Court, it redetermined and decided overpayments in income tax of $16,434.02 for the year 1962, $121,571.00 for the year 1963 and $156,322.58 for the year 1964.

The taxing statute, Section 6214(a) Internal Revenue Code, vested the Tax Court with jurisdiction, authority and responsibility to redetermine the Commissioner's deficiency determination in the first case. *The LTV Corporation* (7/21/75) 64 T.C. No. 59; (judgment from Commissioner's

concession); *Ross Bowman* (1951) 17 T.C. 681 (judgment from Commissioner's waiver[6] and disclaimer).

In *The LTV Corporation, supra,* the Tax Court stated:

"We agree with petitioner that respondent's concession of no deficiency does not deprive us of jurisdiction over the subject matter. It would be anomalous in the extreme if respondent's concession on the merits deprived the Court of jurisdiction to enter a decision in favor of petitioner. As we said in Daniel E. Hannan, 52 T.C. 787 791 (1969):

> [I]t is not the existence of a deficiency but the Commissioner's determination of a deficiency that provides a predicate for Tax Court jurisdiction . . . Indeed, were this not true, then the absurd result would be that in every case in which this Court determined that no deficiency existed, our jurisdiction would be lost.

Having acquired jurisdiction, this Court has the authority and responsibility to enter a decision on the merits. Ross Bowman, 17 T.C. 681 (1951) . . . But section 6214(b) simply makes unmistakably clear what is contemplated by the jurisdiction conferred in section 6214(a) and the two preceding sections: that this Court's jurisdiction is limited to a redetermination of the correct amount of the deficiency, if any, for the years for which the deficiency notice specified in section 6212 has determined a deficiency as defined in section 6211."

In the referred to case of *Ross Bowman, supra,* at pages 685-686, the Tax Court stated:

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[6]waiver is a synonym of abandon

"Having unquestionably obtained jurisdiction for 1943, this Court may not be ousted from that status by action of the respondent nor deprived of its right to enter a final decision with respect to the petitioner's tax liability for that year. The reason for this rule is clear. A litigant in a matter before a court of competent jurisdiction who brings the other party into court is entitled to an ultimate judgment, and the opposing party cannot defeat the jurisdiction of the court by a waiver or disclaimer on his part. The rule is aptly stated by the Supreme Court in the case of Last Chance Min. Co. v. Tyler Min. Co., 157 U.S. 683, in which it is said:

> . . . When an action has been instituted in the court to determine such a controversy, it is not within the competency of the defendant to take himself out of court. A defendant may withdraw his answer and thus let judgment go by default, but he does not thereby deprive the court of a jurisdiction which has been once established. The rule applicable here is no different from that which applies in any other case. When a defendant has by personal service or appearance once been brought into a court, having jurisdiction of the subject matter, he cannot at his election oust the court of jurisdiction, or prevent the case from passing to judgment. Whether he confesses plaintiff's right or defaults in answer, or files a denial or a disclaimer, is alike immaterial. In each and all of these cases the jurisdiction remains and the court may enter the appropriate judgment. Where the defendant simply withdraws his answer, as was this case, the court is under no obligations to inquire whether he has lost all interest, but may proceed to judgment, and its judgment is an adjudication of the rights of the plaintiff, as shown by the complaint and testimony . . .

Here, after trial in the first case, the Commissioner's decline to brief the facts of record and the law in defense of his overhead deficiency determination and his abandonment of the overhead issue in the first case, has the sameness of a decline to continue to proceed in defense of his deficiency determination, to a disclaimer, to a waiver, to a default and to a concession of the overhead issue. *Last Chance Min. Co.* v. *Tyler Min. Co.* (1895) 157 U.S. 683.

Rule 123(d) of the Rules of Practice and Procedure United States Tax Court (Appendix H, p. 123a, infra) reads:

> "Effect of Decision on Default . . . A decision rendered upon a default . . . shall operate as an adjudication on the merits."

Here, the Tenth Circuit Court of Appeals Opinion that there was neither a judicial determination nor a judgment on the merits of the overhead issue in the first Tax Court case because of the Commissioner's abandonment of the issue after trial, conflicts with the aforesaid Rule 123(d) of the Rules of Practice and Procedure of the United States Tax Court.

Conclusion. It follows that Tax Court Judge Murdock's Opinion and Decision in the first case, contrary to the Tenth Circuit Court of Appeals holding, was a judicial redetermination and a final judgment on the merits of the overhead issue against the Commissioner and for Coors. Section 6214(a) Internal Revenue Code; *The LTV Corporation, supra,* (judgment from Commissioner's concession); *Ross Bowman, supra,* (judgment from Commissioner's waiver

and disclaimer); *Thomas A. Shaheen, Jr.* (1974) 62 T.C. 359 (Judgment by default); *Last Chance Min. Co. v. Tyler Min. Co., supra,* (judgment for plaintiff from defendant's default, disclaimer and abandonment); *U. S. v. Zimmerman* (CA-7, 1973) 478 F.2d 59 (judgment from agreement of Commissioner and taxpayers); *Olsen v. Muskegan Piston Ring Co.* (CA-6, 1941) 117 F.2d 163 (judgment from default); and *Bettcher v. State of Colorado* (En Banc, Colo. Sup. Ct., 1959) 344 P.2d 969 (judgment from default and defendant's decline to pursue its defense).

The Tenth Circuit's inference that Judge Murdock's Opinion and Decision in the first case was not a judgment on the merits conflicts with the above taxing statute, Tax Court cases, Circuit Court of Appeals cases, and cases of the Colorado Supreme Court and the United States Supreme Court.

The Opinion and Decision of Tax Court Judge Murdock was a final valid judgment as to all matters of fact and law of the overhead issue that were or should have been adjudicated in the first case. *Morris v. Jones* (1947) 328 U.S. 545.

The guidelines underlying the doctrine of res judicata and collateral estoppel were finalized by the Supreme Court in *CIR v. Sunnen* (1948) 333 U.S. 591, 597 as follows:

> "The general rule of res judicata applies to repetitious suits involving the same cause of action. It rests upon considerations of economy of judicial time and public policy favoring the establishment of certainty in legal relations. The rule provides that when a court of competent jurisdiction has entered a final judgment on the merits of a cause of action, the parties to the suit and their privies are thereafter bound 'not only as to every matter which was offered and received to sustain or defeat the claim or demand, but as to any other admissible matter which might have been offered for that purpose.' Cromwell v. County of Sac, 97 U.S. 351, 352. The judgment puts an end to the cause of action, which cannot again be brought into litigation between the parties upon any ground whatever, absent fraud or some other factor invalidating the judgment."

Accordingly, it is submitted for purposes of the application of res judicata and collateral estoppel, the question of whether Judge Murdock's Tax Court Opinion and Decision of the overhead issue in the first case was a judicial redetermination and a judgment on the merits involves a federal taxing statute (Section 6214(a) IRC) of national importance, which federal question is so substantial that it should be absolutely resolved and settled by this Court.

II

THE OPINION OF THE TENTH CIRCUIT COURT OF APPEALS IN HOLDING THAT RES JUDICATA AND COLLATERAL ESTOPPEL DOESN'T APPLY, BASED UPON ITS ERRONEOUS PREMISE "THERE WAS NO JUDICIAL DETERMINATION" OF THE OVERHEAD ISSUE AND IT "WAS NOT JUDICIALLY DETERMINED" AND ITS ERRONEOUS INFERENCE THERE WASN'T A JUDGMENT ON THE MERITS IN THE FIRST CASE, CONFLICTS WITH DECISIONS OF THE SEVENTH AND SIXTH UNITED STATES CIRCUIT COURT OF APPEALS: U. S. V. ZIMMERMAN, SUPRA (JUDGMENT FROM AGREEMENT) AND OLSEN V. MUSKEGAN PISTON RING CO., SUPRA, (JUDGMENT FROM DEFAULT).

In *U. S. v. Zimmerman, supra,* where the Tax Court entered decisions for joint income taxes and penalties against a husband and wife based upon agreement of the parties, the

Seventh Circuit held the doctrine of res judicata to the applicable.

Olsen v. Muskegan Piston Ring Co., supra, was a case to compel the issuance of stock and for an accounting. At the trial Olsen declined to proceed and the company presented testimony. The Trial Court entered an order of dismissal with prejudice. There the Sixth Circuit Court of Appeals, in holding that the judgment of the Trial Court was rendered on the merits, said:

> "Appellants' contention that no judgment was rendered on the merits also is not tenable. A judgment on the merits does not require a determination of the controversy after a trial or hearing on controverted facts. It is sufficient if the record shows that the parties might have had their controversies determined according to their respective rights if they had presented all their evidence and the court had applied the law. Freeman on Judgments, 5th Ed., Vol. II, s823-725. Such an opportunity was afforded the appellant, who did not avail himself of the right. Under such circumstances the dismissal with prejudice is justified."

In the instant first case, after a full adversary trial on the merits between Coors and the Commissioner, Coors filed its brief with the Tax Court. The Commissioner declined and defaulted upon his obligation and right to brief the defense of his overhead determination. The Commissioner in his brief stated that he now abandons the several adjustments of his overhead issue determination. The Tax Court in its Opinion and Decision made findings of fact and ultimate conclusions of the several overhead adjustments issue. The Tenth Circuit's Opinion here that Judge Murdock's Opinion and Decision was not a judicial redetermination of the overhead issue because of the Commissioner's abandonment is

untenable and in conflict with the Sixth Circuit Court of Appeals judgment in *Olsen v. Muskegan Piston Ring Co., supra.*

Res Judicata. In the first case the Commissioner's determined overhead issues for the years 1962, 1963 and 1964 were redetermined by the Tax Court for Coors. Contrarily, in the instant second case the Commissioner again determined the same overhead issues for the years 1962, 1963 and 1964 for purposes of making his computations and determination under Section 481 of the Internal Revenue Code. Accordingly, the Tenth Circuit Court of Appeals denial of the application of the doctrine of res judicata incident to the Commissioner's Section 481 overhead adjustment in the instant second case conflicts with the cases of Hyman v. Regenstein (CA-5, 1958) 258 F.2d 502, cert. den'd. 359 U.S. 913 and Evergreens v. Nunan (CA-2, 1944) 141 F.2d 927-928, cert. den'd. 323 U.S. 720.

Accordingly, it follows that the Tenth Circuit's holding that res judicata and collateral estoppel doesn't apply, based upon its erroneous premise the overhead issue "was not judicially determined" and its erroneous inference there wasn't a judgment on the merits in the first case, also conflicts with the aforesaid cases of the Seventh and Sixth United States Courts of Appeal, *U. S. v. Zimmerman, supra,* and *Olsen v. Muskegan Piston Ring Co., supra.*

The Tenth Circuit's holding that the doctrine of res judicata is inapplicable equally conflicts with the decisions of *Hyman v. Regenstein, supra;* and *Evergreens v. Nunan, supra.*

In view of the aforesaid conflicts between the several Circuit Courts of Appeals, it is submitted that certiorari should be granted and the issue finally resolved and decided by the United States Supreme Court.

III

WHERE THE PARTIES AND THE OVERHEAD ISSUE WERE THE SAME IN THE PRIOR FIRST CASE AND THE INSTANT SECOND CASE AND WHERE THE OPINION AND DECISION OF THE TAX COURT IN THE PRIOR FIRST CASE CONSTITUTED A FINAL JUDGMENT ON THE MERITS, THE TENTH CIRCUIT OPINION THAT THE DOCTRINE OF RES JUDICATA AND COLLATERAL ESTOPPEL IS NOT APPLICABLE AND DISPOSITIVE OF THE OVERHEAD ISSUE IN THE INSTANT SECOND CASE CONFLICTS WITH THE DECISIONS OF THE U.S. SUPREME COURT.

In *Blander-Tongue Laboratories, Inc. v. University of Illinois Foundation, et al* (1971) 402 U.S. 313, a patent infringement case, the Supreme Court listed with approval the following criteria for application of the doctrine of res judicata and collateral estoppel or estoppel by judgment:

> "In determining the validity of a plea of res judicata three questions are pertinent: Was the issue decided in the prior adjudication identical with the one presented in the action in question? Was there a final judgment on the merits? Was the party against whom the plea is asserted a party . . . to the prior adjudication? 19 Cal. 2d, at 813, 122 P.2d, at 895."

1. SAME PARTIES. Here the parties in the first and second Tax Court cases were the same.

2. SAME ISSUE. The overhead issue decided by the Tax Court against the Commissioner and for Coors in the first case is identical with the overhead issue decided for the Commissioner in the instant second case by the Tax Court and affirmed by the Circuit Court of Appeals, Tenth Circuit.

3. A FINAL JUDGMENT ON THE MERITS. The third and crucial question is whether there was "a final judgment on the merits" by the Tax Court of the overhead issue in the first case.

In the first case there was a full and complete trial on the merits by the litigating parties of the overhead issue. After trial, Coors filed its Tax Court brief setting forth the facts, law and argument to support its request that the Tax Court redetermine the overhead issue for Coors. The Commissioner in his brief declined, defaulted and waived his right and obligation to continue to defend his overhead deficiency determination and therein he stated that he now abandons[6] the issue.

Judge Murdock entered his Tax Court Opinion finding and holding that:

> "The Commissioner in his brief abandons the disallowances of deductions made in the deficiency notice of $405,567.07 for 1962, $560,942.25 for 1963 and $310,866.81 for 1964 representing corporation costs of construction overhead and maintenance and costs of engineering department overhead. He also abandons disallowances of $59,-009.60 for 1962, $95,931.71 for 1963 and $122,-076.56 for 1964 representing depreciation of construction equipment of the corporation."

The Commissioner then filed his computation with the Tax Court showing findings of overpayments in income taxes for each of the years 1962, 1963 and 1964. The Commissioner's computation also found as facts the amounts of expenses reported by Coors, which were disallowed and determined by the Commissioner to be non-deductible overhead costs and now abandoned by the Commissioner for the years 1962, 1963 and 1964.

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[6]Abandon is a synonym of "waiver" and "waive". See definitions of "waiver" and "waive" in Webster's Collegiate Dictionary, Third Edition, 1925 and 1959 Editions. The same dictionaries define abandon "to give up with the intent to never again claiming one's rights or interest in, to give over or surrender completely."

Thereupon Judge Murdock entered his Tax Court Decision, incorporating the findings stated in the Commissioner's computation as the findings of the Tax Court, and redetermining overpayments in income tax of $16,343.02 for 1962, $121,571.00 for 1963 and $156,322.58 for 1964.

Accordingly, it is submitted, Judge Murdock's Opinion and decision redetermining income tax overpayments for the years 1962, 1963 and 1964 was a judgment on the merits and that the Tenth Circuit Court of Appeals erred in not invoking the doctrine of res judicata and collateral estoppel.

In conclusion, we submit that the Opinion and judgment of the Tenth Circuit Court of Appeals, in holding that res judicata and collateral estoppel is inapplicable, conflicts with case law, the long established doctrine of res judicata and collateral estoppel and is in direct conflict with U.S. Supreme Court cases and other Circuit Court of Appeals cases. *Blander-Tongue Laboratories, Inc. v. University of Illinois Foundation, et. al., supra; Last Chance Min. Co. v. Tyler Min. Co., supra* (judgment from defendant's abandonment, default and disclaimer); *U. S. v. Zimmerman, supra,* CA-7, (judgment from agreement); *Olsen v. Muskegan Piston Ring Co., supra* CA-6 (judgment from default); *Fairmont Aluminum Company v. CIR* (CA-4, 1955) 222 F.2d 622, cert. den'd. 350 U.S. 838 (judgment upon failure of proof); *James Talcott v. Allanhabad Bank Ltd.* (CA-5, 1971) 444 F.2d 451, cert. den'd. 404 U.S. 940.

CONCLUSION

For the foregoing reasons, the Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX

APPENDIX A

T. C. Memo. 1968-256

TAX COURT OF THE UNITED STATES

ADOLPH COORS CO., ADOLPH COORS, JR., AND MAY KISTLER COORS, JOSEPH COORS AND HOLLY H. COORS,

Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*

Docket Nos. 3179-66, 3180-66, 3181-66.

Filed November 7, 1968.

Gene W. Reardon, for the petitioners.

Richard J. Shipley, for the respondent.

MEMORANDUM FINDINGS OF FACT AND OPINION

The Commissioner determined deficiencies in income tax of the petitioners as follows:

Year	Adolph Coors Co.	Adolph Coors, Jr. & May Kistler Coors	Joseph and Holly H. Coors
1962	$1,515,137.09	$7,650.00	$4,919.99
1963	873,545.20	7,650.00	5,933.27
1964	4,213,516.29	6,705.00	6,334.63

The issues requiring decision in the corporation case are:

1. Were the earnings of the company accumulated in each year beyond its reasonable needs to avoid tax on its shareholders,

2. Did two beer cellars and four barley receiving stations qualify as "Section 38 property" for investment credit purposes, and

3. Are costs of repairs and utilities on house No. 1 and depreciation on houses Nos. 1 and 2 deductible.

The issues for decision in the cases of the individuals are:

1. Did the Commissioner err by including in income rental values of houses belonging to the company and occupied by the petitioners, and

2. Was a fee paid by Joseph to an attorney to apply for and receive a patent deductible as a business expense.

Paragraphs 29 and 40 of the stipulation are agreements to two adjustments favoring the corporation.

The Commissioner in his brief abandons the disallowances of deductions made in the deficiency notice of $405,567.07 for 1962, $560,942.25 for 1963 and $310,866.81 for 1964 representing corporation costs of construction overhead and maintenance and costs of engineering department overhead. He also abandons disallowances of $59,009.60 for 1962, $95,931.71 for 1963 and $122,076.56 for 1964 representing depreciation on construction equipment of the corporation.

FINDINGS OF FACT

Adolph Coors Co. (hereinafter referred to as the corporation) is a Colorado corporation. Its principal place of business at all times material hereto was at Golden, Colorado. Its federal income tax returns for the years 1962, 1963 and 1964 were filed with the district director of internal revenue at Denver, Colorado.

Adolph Coors, Jr. and May Kistler Coors are husband and wife and their legal residence at all times material hereto was Golden, Colorado. They filed joint federal income tax returns for the years 1962, 1963 and 1964 with the district director of internal revenue at Denver, Colorado.

Joseph Coors and Holly H. Coors are husband and wife and their legal residence at all times material hereto was Golden, Colorado. They filed joint federal income tax re-

turns for the years 1962, 1963 and 1964 with the district director of internal revenue at Denver, Colorado.

The deficiency notice to Adolph Coors Co. first states the deficiencies determined as listed above. Then the following is the first paragraph of the text of that document:

> In accordance with the provisions of existing internal revenue laws, notice is given that the determination of your income tax liability for the above-noted taxable year(s) discloses a deficiency (or deficiencies) in the amount(s) shown above. The attached statement shows the computation of the deficiency or deficiencies.

The computations in "The attached statement" show for each year how those deficiencies were computed and also show how an accumulated earnings tax for each year was computed. "The attached statement" also contains a paragraph as follows:

> It is determined that for each of the years ending December 31, 1962, 1963 and 1964, you were formed or availed of for the purpose of avoiding the income tax with respect to your shareholders by permitting earnings and profits to accumulate instead of being divided or distributed. Accordingly, the accumulated earnings tax as provided by section 531 of the Internal Revenue Code is asserted for each of those years.

The amounts "asserted for each of those years" were $1,245,-567.97 for 1962, $560,073.37 for 1963 and $4,076,129.43 for 1964.

The Commissioner, in computing the income tax deficiencies and the "asserted" accumulated earnings tax against the corporation for each year, used the following amounts as the

corporation's taxable income and accumulated earnings tax net income:

Year	Taxable Income	Accumulated Earnings Tax Net Income
1962	$20,210,906.60	$ 3,263,812.91
1963	21,657,879.44	1,483,307.46
1964	27,723,068.14	10,615,920.59

All of the above amounts are erroneous and their use by the Commissioner in determining the deficiencies and "asserting" the accumulated earnings taxes resulted in the determination of erroneous deficiencies and in the assertion of erroneous accumulated earnings taxes.

William K. Coors and Joseph Coors are sons of Adolph Coors, Jr.

The principal officers of the corporation during the tax years were: William K. Coors, president and chairman of the board; Joseph Coors, executive vice president; Adolph Coors, Jr., treasurer; and Ray V. Frost, financial vice president and secretary. These officers and Herman F. Coors, now deceased, comprised the Board of Directors. Herman F. Coors resided in Arizona.

The capital stock of the corporation as of December 31, 1964 was as follows:

	Authorized	Treasury	Outstanding
Class A voting common stock ($100 par value)	12,000	687	11,313
Class B, no par, non-voting common stock	440,000	30,054	409,946

This capital stock structure remained unchanged throughout the years 1962, 1963 and 1964 with the exception of a redemption by the corporation for $507,500 of 7,000 shares of Class B stock from the Bertha Coors Monroe Estate in

October 1963. A preferred stock dividend of $10,000,000 was issued in 1951 by the corporation to holders of the common stock. A preferred stock dividend of $1,000,000 was issued to holders of preferred stock in 1957. The capital stock was thereafter issued under a 1959 plan of recapitalization in which the corporation's common stock was reclassified as Class A common stock and its preferred stock was changed into Class B common stock.

The corporation had the right under its Articles of Incorporation and By-laws of first refusal to purchase at market value any of its outstanding shares of capital stock which were being offered for sale.

All of the outstanding shares of Class A common stock were held in trust during the tax years under a trust agreement executed on January 7, 1922. That agreement as amended provides that the trustees shall have and exercise the voting powers with respect to the Class A stock. The amendment to the said trust agreement dated July 10, 1959 contains the following statement as to purpose of the trust:

> WHEREAS the intention and purposes of said trust agreement as amended were and this amendment is to unify, protect, preserve, and develop to the greatest possible advantage and benefit the interests of the members of the Adolph Coors family as the beneficiaries under said Trust Agreement as Amended, and to that end to preserve the continuity of management and of the managing personnel of Adolph Coors Co. * * *

The shareholders were given trust receipts in place of their capital stock, and the corporation had the right of first refusal to purchase any trust receipts being offered for sale.

Trust receipts representing beneficial interests in the shares of Class A stock were held as follows during 1962:

William K. Coors	1,625 shares
Joseph Coors	1,625 shares
Adolph Coors, Jr., as Trustee of 1923 Trust of Adolph Coors	4,500 shares
Trustees of Trust of Adolph Coors, Jr.	1,750 shares
Trustees of Trust of Grover C. Coors	1,063 shares
Trustees of Trust of Bertha Coors Monroe	750 shares
Total	11,313 shares

The trustees under said trust during the tax years were: Adolph Coors, Jr., Herman Coors, William K. Coors and Joseph Coors. Those holdings continued throughout the tax years except that in about March 1963 the 750 shares of the trust of Bertha Coors Monroe were purchased equally by William K. Coors and Joseph Coors.

The following Class B shares of the corporation were held as of December 31, 1964 in the following amounts by trusts (created in the years indicated) of Adolph Coors and the Trusts of the latter's three sons and three daughters:

Adolph Coors (1923)	165,004 shares
Adolph Coors, Jr. (1946)	64,168 shares
Grover C. Coors (1952)	37,860 shares
Herman F. Coors (1946)	65,914 shares
Augusta Coors Collbran (1946)	28,250 shares
Bertha Coors Monroe (1946)	16,500 shares
Louise Coors Porter (1946)	28,250 shares
Total	405,946 shares

All of those trusts, except the irrevocable trust created by Adolph Coors of which Adolph Coors, Jr. is sole trustee, were created as revocable trusts but they have or will become irrevocable upon the death of the respective settlors. The trustees of the six trusts are the same individuals as the trustees of the 1922 Voting Trust, except that Adolph Coors, Jr. is not a trustee of his own trust and Herman F. Coors was not a trustee of his trust. The beneficiaries of each of the Class B trusts are either the respective settlors or their relatives. William K. Coors and Joseph Coors each owned 2,000 Class B shares on December 31, 1964 which they obtained from the Estate of Bertha Coors Monroe in 1963. Apart from this transfer and the redemption in 1963, the Class B shareholdings continued unchanged throughout the years involved.

The brewery business was started in 1873 by Adolph Coors and in 1913 it was incorporated under the laws of Colorado. The principal business of the corporation is the production and sale of beer and malt. The ingredients of its beer are Rocky Mountain Spring Water, hops, barley and rice. The Rocky Mountain Spring Water is obtained from wells drilled by the corporation on land in the vicinity of Golden, Colorado. The corporation purchases most of its hops which are grown in the Bavarian section of Western Germany. It buys from farmers and conditions its barley within the State of Colorado. It purchases its rice, which is grown principally in California. The finished beer is placed in bottles, cans and kegs at the Golden plant, from where it is promptly shipped, either by railroad car or truck, and sold to its 180 distributors throughout eleven Western States of the United States.

The corporation employs numerous engineers, and it conducts its own planning, designing, development and architectural work at its brewery plant. Many of the planned projects of the engineers are scrapped and abandoned. The corporation's expansion projects are planned months to years in advance of the actual starting. The corporation erects buildings and other physical structures, as additions to its brewery plant, from the plans drafted and approved by its engineers and management. The corporation uses its own equipment and work force to build these structures, and it does its own repair and maintenance work. The corporation also designs, builds and installs machinery and equipment which are used in the operation of its brewery plant. The corporation owns and operates a very modern, complete and independent brewery plant.

The corporation has limited storage facilities for its packaged beer, and consequently its beer is mostly shipped to its distributors as soon as it is packaged in kegs, bottles or cans.

There were 750 breweries in the United States in the late 1940's and only 93 in 1968. The corporation ranked tenth in volume of sales among the nation's brewing companies in 1966 and in 1967 it moved into seventh position. Most of the breweries which rank ahead of the corporation sell their products nationwide and have branch production plants. Adolph Coors Co. has only one production plant.

The corporation has not increased the sales price of its beer to its distributors in the last 20 years.

The corporation's comparative balance sheets for the ends

of the taxable years 1962, 1963 and 1964 disclose the following:

ASSETS	1962	1963	1964
Cash	$10,256,797	$ 8,740,398	$13,806,244
Tax Ant. Cert.*	2,477,756	2,505,000	8,000,000
Trade Accts. Rec.	3,188,548	3,135,605	3,505,904
Inventories	11,131,945	14,293,912	17,517,935
Prepaid and deferred Charges	278,183	248,047	154,476
Total Current Assets	$27,333,229	$28,922,962	$42,984,559
Investment in Corporate Securities	793,100	735,866	733,196
Prepayment on Stock Redemption	758,475	94,411	555,939
Fixed Assets	38,276,110	47,081,160	48,841,371
TOTAL ASSETS	$67,160,914	$76,834,399	$93,115,065
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current Liabilities	9,589,231	9,766,367	12,391,315
Non-current Liabilities	965,000	804,433	643,922
Stockholders' Equity	56,606,683	66,263,599	80,079,828
TOTAL	$67,160,914	$76,834,399	$93,115,065
WORKING CAPITAL (Current Assets less Current Liabilities)	$17,743,998	$19,156,595	$30,593,244
NET LIQUID ASSETS (All Cash less Current Liabilities)	$ 3,145,322	$ 1,479,031	$ 9,414,929

The demand for Coors beer has constantly exceeded production. Each year there has been an expansion of facilities, an increase in beer production and an increase in sales of 10 to 13 percent over the previous year.

The beer production and sales of the corporation have increased from 811,995 barrels in 1953 to 2,772,309 barrels in 1962, 3,053,241 barrels in 1963 and 3,421,132 barrels in

*U.S. Government Securities or Cerificates of Deposit.

1964. Gross profits increased during this period from $7,-811,739 in 1953 to $26,223,855 in 1962, $28,345,824 in 1963 and $32,790,993 in 1964.

The corporation continuously carries on a current and a future building and plant expansion program to meet the annual increased demand for its products. This expansion program is carried out without any interruption of the brewery's current output of beer. The expansion program is financed solely from accumulated earnings. The corporation does not borrow any money. The extent of the expansion each year is limited to the corporation's accumulated earnings and its available cash on hand. Its cash position is always low in the early months of each year, particularly in March. Early in 1964 the Board of Directors became alarmed over the corporation's low cash position and caused a temporary curtailment in expansion expenditures but later in 1964 there was a sufficient accumulation of cash to accelerate its construction expansion. The corporation does not and cannot rely solely on future earnings to finance its planned expansion projects because of the uncertainty of the level of such earnings.

The following schedule shows the corporation's cash position including bank balances and U.S. Certificates of Indebtedness as of quarterly dates during the tax years:

Date	Bank Balances	U.S. Cert. of Indebtedness	Total
Jan. 1, 1962	$ 9,095,560.60	$1,966,560.00	$11,062,120.60
Mar. 31, 1962	4,488,256.31	1,977,517.22	6,465,773.53
June 30, 1962	6,825,153.56	1,490,270.00	8,315,423.56
Sept. 30, 1962	8,323,399.25	1,986,250.00	10,309,649.25
Dec. 31, 1962	10,256,797.04	2,477,755.56	12,734,552.60
Mar. 31, 1963	7,197,159.67	2,476,973.61	9,674,133.28
June 30, 1963	8,122,661.03	2,482,896.53	10,605,557.56
Sept. 30, 1963	7,621,834.05	2,500,000.00	10,121,834.05
Dec. 31, 1963	8,738,381.79	2,505,000.00	11,243,381.79
Mar. 31, 1964	5,502,880.42	2,700,000.00	8,202,880.42
June 30, 1964	9,477,028.61	3,000,000.00	12,477,028.61
Sept. 30, 1964	15,566,516.36	3,000,000.00	18,566,516.36
Dec. 31, 1964	13,806,244.02	8,000,000.00	21,806,244.02

The expansion of the brewery facilities and the increase in beer production requires additional cash for increases in inventories and accounts receivable and proportionately increased operating expenditures.

The corporation neither carries insurance nor does it maintain cash reserves to cover losses from fire, casualty, crop losses, spoilage losses, business interruption losses, or other risks and hazards.

A $14,000,000 civil suit for breach of contract was filed against the corporation in the Denver District Court on March 5, 1964. The corporation is not insured against any judgment and does not have any cash reserve set aside therefor.

The corporation would like to acquire additional water rights and additional land should either become available.

The corporation needs substantial amounts of cash on hand to pay its federal excise taxes for which liability is incurred as the beer is shipped.

The corporation has never made any loans to its stockholders and none of its accumulated earnings for the taxable years were invested in nonbusiness assets.

The corporation, during the tax years, commenced or had committed itself to 33 building projects. It worked on 22 of them in 1962 and the remaining cost, at the end of 1962 on those to which it was then committed, was $35,343,000.

It completed 6 in 1963 and worked on 22 others. The remaining cost, at the end of 1963 on those to which it was then committed, was $28,391,000.

It completed 5 in 1964 and worked on 20 others. The remaining cost, at the end of 1964 on those to which it was then committed, including the aluminum can plant, was $48,055,-000. At that time it knew that the cost of land for the can

plant would be $1,500,000 and that the plant would need $2,400,000 for aluminum cooperage.

The corporation paid federal and state taxes of over $119,000,000 during the tax years. It paid $5,909,682.20 in 1963 with the filing of its federal income tax return for 1962, $5,540,343.28 in 1964 for 1963 and $7,075,674.44 in 1965 for 1964. It also filed and paid substantial taxes on its declaration of estimated tax for each year, including the year 1965.

The corporation had no accumulated earnings beyond the reasonable needs of its business at the end of any of the years 1962, 1963 or 1964.

The total dividends paid by Adolph Coors Co. were as follows:

Year	Dividends Paid
1962	$513,910.80
1963	511,810.80
1964	505,510.80

Since its incorporation in 1913 the company policy has been to keep the corporation's stock within the Adolph Coors family. This policy has applied to both the Class A and Class B stock. The purpose of this policy is to avoid letting "outsiders" interfere with the management or learn about company affairs.

The principal shareholders of the corporation or holders of beneficial interests under the various trusts in recent years have been the six sons and daughters of Adolph Coors who died in 1929. The sons were Grover Coors who died in 1954, Herman F. Coors who died in January 1967, and Adolph Coors, Jr. who in 1964 was about 80 years old. The daughters were Bertha Coors Monroe who died in about February 1961, Augusta Coors Collbran who died in about January 1963, and Louise Coors Porter who died in November 1964.

The corporation had owned stock of six companies for many years. None had any relation to its business.

The corporation received income from dividends as follows:

Year	Dividends Paid
1962	$332,741.48
1963	411,768.85
1964	416,364.89

The following table shows the dividends received from the corporation during the tax years and the minimum tax rates at which any additional dividends would have been taxed:

Stockholder	Year	Dividends Received	Maximum Tax Bracket
Adolph Coors, Jr.	1962	$144,646.24	89%
	1963	144,646.24	89%
	1964	142,009.52	76.5%
William K. Coors	1962	1,950.00	84%
	1963	2,887.50	72%
	1964	11,656.88	63.5%
Joseph Coors	1962	1,950.00	72%
	1963	2,887.50	72%
	1964	4,640.00	63.5%
Herman F. Coors	1962	105.312.80	75%
	1963	105,312.80	75%
	1964	102,171.24	66%
Louise Coors Porter	1962	60,116.00	75%
	1963	60,116.00	75%
	1964	44,239.00	58.5%

Cellars 11 and 12 are units. Each is an integral part of the brewery through which the beer flows for the fermentation,

aging, cooling, filtration and clarification stages of production and storage before being packaged for sale. Every detail of each cellar was specially designed and constructed to accomplish the above steps in the production of the finished product. They have no other use.

The corporation constructed a shell and steel supports to enclose and support very large beer tanks and related equipment, all of which was known as Cellar No. 11. Construction on this facility was started in 1961 and completed and put in use in 1963. The corporation expended $612,763.61 in 1962 and $9,734.76 in 1963 on Cellar 11. It is subject to depreciation and it has a useful life of over eight years.

The corporation constructed a similar shell and steel supports to enclose and support beer tanks and related equipment known as Cellar No. 12. Construction on this facility was started in 1962 and was completed and put in use in 1964. The corporation expended $37,693.27 in 1962, $1,443,-182.22 in 1963, and $298,140.88 in 1964 on Cellar 12. It is subject to depreciation and has a useful life of over eight years.

Cellars 11 and 12 are substantially identical. The enclosure for the tanks and equipment of each cellar rests on concrete caissons, which support heavy steel columns. The columns, together with supporting heavy cross beams, support a closely packed honeycomb of 192 large glass-lined metal storage tanks, each weighing 40,000 pounds empty and holding 1,584 barrels of beer. There are a number of levels of horizontal beer storage tanks and a top level (equal to two lower levels) of 50 fermenting tanks within each enclosure. Each fermenting tank has a capacity of 2,000 barrels. Above each fermentor is a stainless steel foam chamber 7 feet high and 12 feet in diameter. The outer wall of each enclosure consist of a four-inch weather barrier insulated by a ten-inch blown glass wool insulation. The top of the enclosure is a

weather protecting cover with a six-inch rigid styro-foam insulation that is supported by and bolted to the top of the fermenting tanks.

The basement of each enclosure contains the ammonia refrigeration system for the tanks. Fans propel the refrigerated air through air ducts at each end of the enclosure, and the refrigerated air circulated through controlled air baffles located at the base of each level of tanks keeps the beer at a controlled temperature.

The highly insulated equipment enclosures of Cellars 11 and 12 were specially designed to accommodate the beer tanks and constitute large refrigeration units, which are absolutely essential to maintain the storage and processing of beer at fixed and controlled temperatures.

The refrigerated and air-cooling systems and the temperature controls of each cellar are checked by an employee two or three times daily while the tanks are filled with beer. Periodically an employee checks the pressure on the tanks and takes beer samples for quality control purposes. Three or four employees are required to fill and empty the beer tanks, and two crews of two employees each clean the empty tanks.

Around and below the tanks in each cellar there is sufficient room for men to tend the equipment and some space below the tanks is used occasionally to store items temporarily.

Cellars 11 and 12 were and are units usable solely for the purposes listed above. Neither is a "building" within the meaning of section 48(a)(1)(B) defining "section 38 property."

One of the most important ingredients of the Coors beer is barley. The corporation years ago obtained seeds of barley from Moravia and has worked since then to improve the grain. It sells the seed to farmers who raise the barley and, if

it meets the Coors test, sell it to the corporation. There is only one crop of the barley grown each year, and it is essential that the corporation have a one-year supply on hand to insure it against a crop failure. The corporation employs 12 agronomists who work closely with the barley farmers. They supervise and control the planting of the seed, the fertilization, irrigation, and the growing of the barley, the harvesting of the grain, and the storage of the barley in the growers' bins. The seed is distributed to the growers in January and March and is planted by April 14. The growing season for the barley is approximately 100 days. It is harvested in August and placed in storage bins of the growers for a three-month rest period to overcome dormancy and develop germination to its highest potential. The barley is shipped by the growers in November and December to the nearest field receiving station of the corporation. There it remains in storage under temperature controls for over one year.

The corporation constructed a receiving station and barley storage facility at Delta, Colorado which was completed in September 1962 and was placed in service in 1962. It is subject to depreciation and has a useful life of more than eight years. The corporation made a capital expenditure of $237,-000.26 in 1962 on the construction of this facility.

The corporation constructed a receiving station and barley storage facility at Monte Vista, Colorado. It was started in 1962 and completed and put in use in 1963. The corporation expended $211,207.76 in 1962, $613,828.16 in 1963 and $3,245.46 in 1964 on the construction of this facility. It is subject to depreciation and has a useful life of more than eight years.

The corporation started, constructed, completed and put in use a barley receiving station and storage facility at Montrose, Colorado in 1963. The corporation expended $95,-310.29 in 1963 in constructing this facility, which is subject to depreciation and has a useful life of over eight years.

The corporation started construction in 1963 and completed and put in use in 1964 a barley receiving station and storage facility at La Jara, Colorado. The corporation expended $2,409.81 in 1963 and $59,506.56 in 1964 in constructing this facility, which is subject to depreciation and has a useful life of over eight years.

The facilities at Delta and Monte Vista are essentially similar, although the Monte Vista facility is larger. The Delta storage facility is 100 feet wide and 221 feet long. The storage capacity is 500,000 bushels. The structure has reinforced tapered concrete walls and is covered with a sheet metal roof. It has two conveyor systems, one located in a gallery or monitor at the peak of the roof for loading grain into the bins and another conveyor system located in a tunnel beneath the floor which is used for emptying the bins. There are walkways along each of the conveyor systems by which employees may operate the equipment and service it. There is a mechanical bay area located at the end of the station which is 21 feet by 100 feet in size. This contains cleaning and elevating equipment. At the end of the station next to the mechanical bay area is a structure in which is located the grain temperature controls and thermo-couple temperature indicators, and also the truck scale dials.

The grain storage facility located at Monte Vista, Colorado is essentially the same as that at Delta. It is, however, considerably larger; it is 110 feet wide and 860 feet long and consists of two wings, 400 feet long, which are divided by a mechanical bay area in the middle which measures 60 feet by 165 feet. This facility has the same type of equipment as the Delta facility.

The facilities at Delta and Monte Vista are designed to receive, weigh, clean, store, and later load for shipment to Golden, barley grown in the respective areas of the state. During the fall or winter when the facilities are receiving grain, normally three employees will be there. Later, during

the storage period, one man will visit the facility periodically. When the grain is shipped out, one man can ordinarily perform that function.

The Montrose and La Jara facilities are essentially the same. They differ from the Delta and Monte Vista facilities in that they are receiving stations where grain can be weighed, received and stored temporarily in a hopper, which is located above a railroad track. The barley then is sent on to either Delta or Monte Vista. The primary difference is that the Montrose and La Jara stations have only temporary storage facilities. Montrose and La Jara have enclosed spacing for reading the truck weighing scale dial and for operating the truck lift. During the harvest season these stations are normally operated by two employees.

After one year, the aging and storage period at the field receiving station, the barley is shipped to the corporation's brewery plant in Golden. There it is processed into malt in one of the corporation's malt houses. The malting process consists of spreading out the barley in compartment beds, mixing it with water for further germination, and later putting the mixed barley through a roasting process. Then the malt is placed in storage for an aging period. The one-day brewing process follows and then the beer is transferred to the cellars.

House No. 1 on the brewery premises was owned by the corporation and occupied during the tax years by the corporation's treasurer, Adolph Coors, Jr. and his wife. Depreciation on that house of $9,377.54 for 1962, $12,110.66 for 1963 and $12,161.85 for 1964 was sustained. The Commissioner in the notice of deficiency disallowed that depreciation.

The corporation also has owned and maintained house No. 2 on its brewery premises. That house has been occupied since 1953 by its executive vice president, Joseph Coors, and his family. Depreciation on that house of $3,127.91 for 1962,

$4,839.39 for 1963, and $5,027.17 for 1964 was sustained. The Commissioner disallowed that depreciation in the notice of deficiency.

The Commissioner estimated utility expenses (one-half for each house) for the two aforesaid houses furnished by the corporation to be $2,400 for each year and added $2,400 to the taxable income of the corporation for each year. The utilities for the house occupied by Joseph were paid for by Joseph and were furnished by the Public Service Co. of Colorado. Those expenditures were not deducted by the corporation on its federal income tax returns. The utilities for the house occupied by Adolph Coors, Jr. were supplied by the corporation's power plant.

The corporation had commenced the construction of cellar No. 11 in 1961 and to provide space for it, the property designated as Residence No. 1 was moved a short distance. The cost of salaries, wages and materials for repairs in 1962 incident to the house move amounted to $60,421.50. The corporation expended in 1963 and 1964 additional amounts of $7,763.15 and $20,372.82 for salaries, wages and materials for repairs in connection with Residence No. 1. Those amounts for each of the three years were added to its taxable income in the notice of deficiency.

The Commissioner in the notice of deficiency determined that house No. 1 had a rental value of $9,000 per year and added that amount as dividend income to the taxable income of Adolph Coors, Jr. for each of the years 1962, 1963 and 1964.

The Commissioner in the notice of deficiency determined that the corporation's house No. 2 had a rental value of $7,-235.29 for 1962, $8,725.39 for 1963 and $8,725.39 for 1964 and added those amounts as dividend income to the taxable income of Joseph Coors for each year.

House No. 1 was old, built in 1880, and was in a very unattractive location for a residence in the brewery complex. It was occupied during the tax years by Adolph Coors, Jr. and his wife and was regularly used on behalf of the corporation for daily luncheons and frequent business meetings. Adolph Coors, Jr. spent most of his time inspecting and checking all parts and activities at the brewery. It was necessary to the performance of his duties for the corporation and required by the corporation that he reside on the premises of the brewery. No amount may be included in his income on account of his occupancy of house No. 1.

The costs of repairs to, utilities for and depreciation on house No. 1 are deductible by the corporation..

House No. 2 was occupied by Joseph Coors and his family. It was newer and was in a much better location than house No. 1. However, it was on the brewery property. Joseph was executive vice president and resident manager of the corporation, was very active in the daily operation of the business of the corporation at the brewery and it was necessary to the performance of his duties for the corporation that he reside at the brewery. The rental value of that residence was not taxable to him as income and the corporation is entitled to deduct depreciation on house No. 2.

Petitioner Joseph Coors paid $1,253.83 which was claimed on his 1964 return as "expenses relative to research and development of a patent of visual and audio language interpreter." The Commissioner disallowed the claimed deduction.

The $1,253.83 included $800 paid to a patent lawyer for obtaining a patent which was granted to the inventor, Paul E. Flury and $450[1] paid to a law firm to form a corporation. Flury worked for Joseph Coors in some way. The evidence does not show that any part of the $1,253.83 was paid as an

[1]Petitioner concedes in his brief that the $450 is not deductible herein.

incident to any business regularly carried on in 1964 by Joseph.

All stipulated facts and exhibits are incorporated herein by this reference.

OPINION

MURDOCK, *Judge:* The Commissioner has "asserted" that the corporation accumulated earnings of each year beyond the reasonable needs of its business and this was done to prevent the imposition of tax upon its shareholders which would have resulted from the payment of larger dividends to the shareholders. He does not claim that the corporation was formed for that purpose but claims it was availed of for that purpose in each tax year.

The Commissioner mailed to the petitioner a notification required by section 534 but the deficiency notice was mailed before the expiration of the 30 days allowed by the Code within which the petitioner could file its statement re accumulated earnings and consequently no statement was filed.

The Commissioner, in the statement attached to the notice of deficiency, "asserted" that the corporation had accumulated income beyond the reasonable needs of its business in the amounts of $3,263,812.91 for 1962, $1,483,307.46 for 1963 and $10,615,920.59 for 1964 and that the accumulated earnings tax thereon was $1,245,567.97 for 1962, $560,-073.37 for 1963 and $4,076,129.43 for 1964. Those assertions are now obviously incorrect because of concessions of the Commissioner in the stipulation and in his brief, by evidence in this case and by the holding of this opinion on several issues which, taken together, reduce the corporate income substantially below the amounts used in the notice of deficiency. The first question relating to each year is — were there actual earnings of each year accumulated beyond the reasonable needs of the business.

The Commissioner makes a computation in his brief in an endeavor to show that the amounts "asserted" as unreasonable accumulations in the statement attached to the deficiency notice are still correct for each year.[2] We have already stated why they are incorrect. Furthermore, nonsequiturs and factual weaknesses on which the Commissioner's reasoning in his brief is based render his conclusions unacceptable for the purpose of this case.

The Commissioner concedes that the petitioner needed a large amount of its current earnings in each year for operating expenses, "working capital." He decides how much by making a complicated computation with a "multiple cycle concept" which computation is not convincing because, as already mentioned, of nonsequiturs and factual weaknesses involved in it. He concludes that the available amounts far exceeded the needs in each year. He unjustifiably belittles too many of the needs of the petitioner for operating expenses, and exaggerates the availability of working capital in his "cycle."

How the need for and availability of funds would coincide or fail to coincide in regard to time during each year was an uncertainty with which the petitioner was annually confronted and with respect to which it will have to be allowed some leeway, particularly as to estimated anticipated needs, in a proper decision here.

The Commissioner also concedes that in determining excessive profits, all amounts actually spent in each year for construction, less allowed depreciation, must be subtracted from current earnings and, he says,[3] they have been subtracted in the deficiency notice in the approximate amounts of $6,300,000 for 1962, $9,000,000 for 1963 and $2,200,000 for 1964. He subtracted nothing for any incomplete

[2]He mentions no lower figures.

[3]It is not clear from the notice of deficiency how much he subtracted but the actual expenditures in 1962 and 1964 were far in excess of the above amounts.

construction or anticipated needs because, he says, all construction "was paid for out of current earnings." Actually construction was paid for out of "accumulated earnings," of which current earnings could become a part only as currently earned during the year.

But in any event section 537, I.R.C. 1954, provides that "the term 'reasonable needs of the business' includes the reasonably anticipated needs of the business." The corporation's operations do not and cannot start and stop at the beginning and end of each year, and it had some large reasonably anticipated needs of its business at the end of each tax year. Work was progressing but was not completed on numerous construction projects in each year. This was particularly true in 1964 when construction was delayed temporarily. It was reasonable to retain a large amount of earnings at the end of each year to assure completion of those projects. Substantial funds would also be needed for anticipated increases in inventories, packaging and other increased production and administration costs. A damage suit for $14,000,000 was instituted against the corporation in 1964. It carried no insurance except against damage to others.

Because of the substantial amount of construction in progress at all times, the corporation's plant has been generally out of balance, as William Coors testified. That is, all parts of a desired increase in production cannot be completed or even started at the same time or even in the same year. But when a project is started its complement must follow as soon as funds and circumstances permit and retention of sufficient current earnings should be allowed for such reasonably anticipated needs at the end of each year, particularly for 1964.

The corporation had, from 1954 to about 1962, been experimenting with the manufacture and use of aluminum cans and had operated a pilot manufacturing plant for four years. Aluminum keeps the flavor of the beer better than cans made

of other metals. The cost of an adequate plant to manufacture aluminum cans had been estimated during the tax years at $20,000,000. It was decided in the summer of 1964 to design and build such a plant but construction was not started until after 1964. However, this plant was a reasonably anticipated need of the business in 1964 and the cost was going to be large. Work on the plant was started and completed after 1964.

Neither party has set forth a computation supported by competent evidence to determine convincingly the reasonable needs of the business or the excess, if any, of earnings over reasonable needs for any year. The evidence shows that this company was continuously expanding rapidly and substantially in order to remain successful in a very competitive business and it needed funds in large amounts to do that. It had to plan well ahead. Its annual earnings had been increasing in most years but its officers and directors were not unreasonable in retaining substantial amounts of current earnings of the tax years for later needs and use.

Beer is a more popular drink in warm weather than in cold. This, no doubt, accounts for the fact that the Coors corporation was lowest in bank deposits in March of each year. The corporation needed funds to carry its operations through the early months of the year when its sales were not bringing in new profits.

A part of the funds required in the early months of 1963, 1964 and 1965 to continue construction in progress but incomplete at the end of each year; a part of the funds needed for reasonably anticipated additional construction at the beginning of each year; funds then needed for operating expenses; funds needed for the payment of state and federal taxes in the early months of 1963, 1964 and 1965; reductions and adjustments resulting from the stipulation, substantially reducing the income shown in the deficiency notice, concessions and holding herein, when combined with deductions

properly recognized in the deficiency notice, leave no accumulations of income beyond the reasonable needs of the corporation's business for any of the years 1962, 1963 and 1964. We hold, after considering all of the facts and circumstances, that for none of the years 1962, 1963 and 1964 were the earnings of the petitioner accumulated beyond its reasonable needs and no accumulated earnings tax is due for those years.

The Commissioner in his brief concedes that the two cellars and the four receiving stations of the corporation "were used as an integral part of its beer manufacturing business" and that the only question is "Do these facilities come within the definition of a building?" Sections 48 and 38, I.R.C. 1954.

Certainly the so-called cellars, numbers 11 and 12 located at the brewery, were important and essential parts of the process used by the corporation in producing its marketable product, beer. Every detail of each was specially designed and constructed for the sole purpose of performing a step in the process of producing the finished product. They had no other use. Beer in a partially finished state flowed into these cellars for the final steps performed by the cellars, fermenting, cooling, aging, filtering, clarifying and storing until the packaging department put the finished beer into kegs, bottles and cans for shipment and sales. These cellars were in no true sense a mere "building" within the meaning of the Code. They were units, each part of which was essential to the whole. Each is an enclosure which is closely combined with the equipment which is a part of it. Even the walls and top of the structure were of a very special design to make the whole an efficient part of the brewery. The cellars were "section 38 property" during the tax years.

The members of the Coors family, who have been responsible for the popularity of their beer and the success of their business, have always regarded the barley grown from the seeds they have developed as one of the most important in-

gredients in the production and popularity of the Coors beer. They develop the seeds for planting and sell them to the barley farmers. The receiving stations have been placed for the convenience of the farmers and have been constructed to receive, store and handle the barley to the best advantage of the corporation. Storage is the main purpose of the receiving stations. The corporation tries to keep available a two-year supply of barley to avoid shortage due to a possible crop failure. The stations are of great importance to the corporation in storing the barley until it is needed for malting at the brewery. The stations have no purpose except those stated herein and were designed and constructed to best accomplish those purposes and no others. The stations were "section 38 property" during the tax years. Cf. *Schuyler Grain Co., Inc.*, 50 T.C. 265; *Robert E. Catron*, 50 T.C. 306.

House No. 1 was old and large for a residence. Its location was most unattractive for a residence. A real estate agent testified that it could not be rented as a residence because of its location. It was occupied by Adolph Coors, Jr. and his wife and was used on behalf of the corporation and was very active in the day to day operation of the brewery. It was important to the corporation and the operation of the business that he reside on the premises. The costs of repairs, utilities and depreciation relating to house No. 1 were deductible by the corporation. No amount should be included in Adolph's income on account of his occupancy of house No. 1.

Joseph Coors occupied house No. 2 so that he could be close to the daily operations at the brewery and readily on call should any emergency arise. The corporation provided the house so that he would be close and would thus benefit the corporation. The agreement had been that he would live there for those purposes. The rental value of the house was not taxable as his income and the corporation is entitled to deduct depreciation on house No. 2.

The record does not provide the Court with factual details from which it could find that Joseph was regularly engaged in any business in which the $800 paid to a patent lawyer was an ordinary and necessary expense.

Decision will be entered under Rule 50.

APPENDIX B

COMPUTATION STATEMENT

CC:DEN-TC:RJS:RDD:ct

In re: Adolph Coors Co.
Golden, Colorado 80401

Docket No. 3179-66

Income Tax
1962

Tax assessed and paid		$9,909,682.20
Payments:		
September 18, 1962	$2,000,000.00	
December 14, 1962	2,000,000.00	
March 15, 1963	2,954,841.10	
June 14, 1963	2,954,841.10	
Total payments	$9,909,682.20	
Tax liability		9,893,248.18
Overpayment		$ 16,434.02

Sections 6512(b)(2)(B) and 6511(b)(2)(A)

Return filed March 15, 1963

No claim filed

Deficiency notice mailed March 14, 1966

1963

Tax assessed and paid		$10,440,343.28
Payments:		
September 18, 1963	$ 2,500,000.00	
December 18, 1963	2,500,000.00	
March 16, 1964	2,720,171.64	
June 12, 1964	2,720,171.64	
Total payments	$10,440,343.28	
Tax liability		10,318,772.28
Overpayment		$ 121,571.00

Sections 6512(b)(2)(B) and 6511(b)(2)(A)

Return filed March 16, 1964

No claim filed

Deficiency notice mailed March 14, 1966

1964

Tax assessed and paid		$12,453,514.44
Payments:		
April 15, 1964	$ 103,420.00	
June 11, 1964	103,420.00	
September 14, 1964	2,585,500.00	
December 14, 1964	2,585,500.00	

1964 Continued

March 16, 1965	$ 3,537,837.22
June 14, 1965	3,537,837.22
Total payments	$12,453,514.44
Tax liability	12,297,191.86
Overpayment	$ 156,322.58

Sections 6512(b)(2)(B) and 6511(b)(2)(A)

Return filed March 15, 1965

No claim filed

Deficiency notice mailed March 14, 1966

The details supporting the above computation are set forth on attached pages 4 through 13, inclusive.

The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that for none of the years 1962, 1963 and 1964 were the earnings of the petitioner accumulated beyond its reasonable needs and no accumulated earnings tax as provided by section 531 of the Internal Revenue Code is due for those years.

The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that Cellars No. 11 and 12 and four barley receiving stations and storage facilities qualify as section 38 property for investment credit purposes during the years 1962, 1963 and 1964.

FORM 3613 (MARCH 1965)	U.S. TREASURY DEPARTMENT - INTERNAL REVENUE SERVICE CORPORATION INCOME TAX	Rule 50 Computation Statement Page 4

NAME	TAXABLE YEARS ENDED		
Adolph Coors Co.	December 31, 1962	December 31, 1963	December 31, 1964
TAXABLE INCOME PREVIOUSLY DETERMINED IN STATUTORY NOTICE DATED March 14, 1966	$ 20,210,906.60	$ 21,657,879.44	$ 25,723,068.14
INCREASES (DECREASES) IN INCOME			
(a) Other expenses — overhead Page 5 for explanation	(405,567.07)	(560,942.25)	(310,866.81)
(b) Depreciation expense Pages 6, 7 & 8 for explanation	(62,912.18)	(58,160.75)	(27,635.66)
(c) Repairs and Maintenance expense Page 9 for explanation	(60,421.50)	(7,763.15)	(20,372.82)
(d) Other deductions Page 10 for explanation	(2,400.00)	(2,400.00)	(2,400.00)
TAXABLE INCOME AS REVISED	$19,679,605.85	$21,028,613.29	$25,361,792.85
TAX COMPUTATION — LESS: EXCESS OF NET LONG-TERM CAPITAL GAIN OVER NET SHORT-TERM CAPITAL LOSS	—	—	219.32
INCOME SUBJECT TO TAX Rate 1962 & 1963 52% less $5,300	$19,679,605.85	$21,028,613.29	$25,361,573.53
PARTIAL TAX: Rate 1964 50% less $7,000 plus Section 1562	$10,227,895.04	$10,929,378.91	$12,675,286.77
ADD: 25% OF EXCESS SHOWN ABOVE *(26% for years beginning before 4/1/54)*	—	—	54.83
SUBTOTAL	$10,227,895.04	$10,929,378.91	$12,675,341.60
LESS TAX CREDITS: Investment Credit See pages 11, 12 & 13	334,646.86	610,606.63	378,149.74
INCOME TAX LIABILITY	$ 9,893,248.18	$10,318,772.28	$12,297,191.86
INCOME TAX PREVIOUSLY ASSESSED Per return	9,909,682.20	10,440,343.28	12,453,514.44
DEFICIENCY (OVERASSESSMENT)	$ (16,434.02)	$ (121,571.00)	$ (156,322.58)

Adolph Coors Co. Rule 50 Computation
Statement Page 5

Explanation of Adjustments

1962

(a) The Commissioner in his brief abandoned the disallowance as operating expenses of costs of construction overhead and maintenance in the amount of $373,-218.74 and costs of engineering department overhead in the amount of $32,348.33. Accordingly, your taxable income is decreased in the amount of $405,567.07.

1963

(a) The Commissioner in his brief abandoned the disallowance as operating expenses of costs of construction overhead and maintenance in the amount of $506,-562.04 and costs of engineering department overhead in the amount of $54,380.21. Accordingly, your taxable income is decreased in the amount of $560,942.25.

1964

(a) The Commissioner in his brief abandoned the disallowance as operating expenses of costs of construction overhead and maintenance in the amount of $241,-115.48 and costs of engineering department overhead in the amount of $69,751.33. Accordingly, your taxable income is decreased in the amount of $310,866.81.

Adolph Coors Co. Rule 50 Computation
Statement Page 6

Explanation of Adjustments

1962

(b) The deduction for depreciation is increased $62,-

912.18 and your taxable income is decreased in a like amount computed as follows:

(1) The Commissioner in his brief abandoned the disallowance of depreciation on construction equipment in the amount of $59,009.60.

(2) The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that $12,505.45 depreciation on residences furnished by the company to Adolph Coors, Jr. and Joseph Coors is an allowable deduction to the corporation.

(3) Due to the adjustments in (a) and (b)(1) above, the additional depreciation of $8,602.87 as computed in the statutory notice is eliminated.

Summary of Adjustment

(1) Depreciation on construction equipment	$(59,009.60)
(2) Depreciation on residences	(12,505.45)
(3) Additional depreciation reversed	8,602.87
Increase depreciation — decrease taxable income	$(62,912.18)

Adolph Coors Co. Rule 50 Computation
Statement Page 7

Explanation of Adjustments

1963

(b) The deduction for depreciation in increased $58,-160.75 and your taxable income is decreased in a like amount computed as follows:

(1) The Commissioner in his brief abandoned the disallowance of depreciation on construction equipment in the amount of $95,931.74.

(2) The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that $16,950.05 depreciation on residences furnished by the company to Adolph Coors, Jr. and Joseph Coors is an allowable deduction to the corporation.

(3) Due to the adjustments in (a) and (b)(1) above, the additional depreciation of $54,721.04 as computed in the statutory notice is eliminated.

Summary of Adjustment

(1) Depreciation on construction equipment	$(95,931.74)
(2) Depreciation on residences	(16,950.05)
(3) Additional depreciation reversed	54,721.04
Increase depreciation — decrease taxable income	$(58,160.75)

Explanation of Adjustments

1964

(b) The deduction for depreciation is increased $27,-635.66 and your taxable income is decreased in a like amount computed as follows:

(1) The Commissioner in his brief abandoned the disallowance of depreciation on construction equipment in the amount of $122,076.56.

(2) The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that $17,189.02 depreciation on residences furnished by the company to Adolph Coors, Jr. and Joseph Coors is an allowable deduction to the corporation.

(3) Due to the adjustments in (a) and (b)(1) above, the additional depreciation of $111,629.92 as computed in the statutory notice is eliminated.

Summary of Adjustment

(1) Depreciation on construction equipment	$(122,076.56)
(2) Depreciation on residences	(17,189.02)
(3) Additional depreciation reversed	111,629.92
Increase depreciation — decrease taxable income	$(27,635.66)

Explanation of Adjustments

1962

(c) The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that costs of repairs in the amount of $60,421.50 incurred in connection with residence No. 1 furnished by the corporation to Adolph Coors, Jr. are deductible. Accordingly, taxable income is decreased in the amount of $60,421.50.

1963

(c) The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that costs of repairs in the amount of $7,763.15 incurred in connection with residence No. 1 furnished by the corporation to Adolph Coors, Jr. are deductible. Accordingly, taxable income is decreased in the amount of $7,763.15.

1964

(c) The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that costs of repairs in the amount of $20,372.82 incurred in connection with residence No. 1 furnished by the corporation to Adolph Coors, Jr. are deductible. Accordingly, taxable income is decreased in the amount of $20,372.82.

Adolph Coors Co. — Rule 50 Computation Statement Page 10

Explanation of Adjustments

1962

(d) The Commissioner in his brief conceded that the utilities expense relating to residence No. 2 furnished by the corporation to Joseph Coors was paid by him individually and was not deducted by the corporation on its federal income tax return.

The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that the utilities expense relating to residence No. 1 furnished by the corporation to Adolph Coors, Jr. is deductible by the corporation.

Due to the above explanations, the statutory notice adjustment of $2,400 to utilities expenses (estimated) is eliminated and taxable income is decreased in a like amount.

1963

(d) The Commissioner in his brief conceded that the utilities expense relating to residence No. 2 furnished by

the corporation to Joseph Coors was paid by him individually and was not deducted by the corporation on its federal income tax return.

The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that the utilities expense relating to residence No. 1 furnished by the corporation to Adolph Coors, Jr. is deductible by the corporation.

Due to the above explanations, the statutory notice adjustment of $2,400 to utilities expenses (estimate) is eliminated and taxable income is decreased in a like amount.

1964

(d) The Commissioner in his brief conceded that the utilities expense relating to residence No. 2 furnished by the corporation to Joseph Coors was paid by him individually and was not deducted by the corporation on its federal income tax return.

The Tax Court of the United States in its opinion T. C. Memo 1968-256, filed November 7, 1968, held that the utilities expense relating to residence No. 1 furnished by the corporation to Adolph Coors, Jr. is deductible by the corporation.

Due to the above explanations, the statutory notice adjustment of $2,400 to utilities expenses (estimate) is eliminated and taxable income is decreased in a like amount.

Adolph Coors Co. — Rule 50 Computation
Statement Page 11

Computation of Investment Credit

1962

Total qualified investment as reported on return		$4,543,669.10
Add: Additional qualified investment Delta, Colorado, receiving station & grain storage facility		237,000.26
Total qualified investment as revised		$4,780,669.36
(1) Tentative investment credit 7%		$ 334,646.86
(2) Limitation Based on Amount of Tax		
		Limitation
Tax from page 2	$10,227,895.40	
Less:	(25,000.00)	$ 25,000.00
Excess: Times 25%	$10,202,895.40	2,550,723.76
Limitation based on amount of tax		$2,575,723.76
Allowable investment credit lesser of (1) or (2) above		$ 334,646.86

Adolph Coors Co. — Rule 50 Computation
Statement Page 12

Computation of Investment Credit

1963

Total qualified investment as reported on return		$6,977,309.06
Add: Additional qualified investment Cellar No. 11		622,498.37
Receiving station and grain storage facility		
Delta, Colorado		2,798.15
Monte Vista, Colorado		825,035.92
Montrose, Colorado		95,310.29
Total qualified investment as revised		$8,522,951.79
(1) Tentative investment credit 7%		$ 596,606.63
Add: Mathematical error on return		14,000.00*
Total tentative credit		$ 610,606.63
(2) Limitation Based on Amount of Tax		
		Limitation
Tax from page 2	$10,929,378.91	
Less:	(25,000.00)	$ 25,000.00
Excess: Times 25%	$10,904,378.91	2,726,094.73
Limitation based on amount of tax		$2,751,094.73
Allowable investment credit lesser of (1) or (2) above		$ 610,606.63

*In the stipulation of facts, it was agreed that Adolph Coors Co. made a mathematical error in computing the investment credit allowable with respect to certain equipment for the Monte Vista elevator.

Adolph Coors Co. — Rule 50 Computation
Statement Page 13

Computation of Investment Credit

1964

Total qualified investment as reported on return		$3,555,218.49
Add: Additional qualified investment Cellar No. 12		1,779,016.37
Receiving station and grain storage facility		
Delta, Colorado		2,742.49
La Jara, Colorado		61,916.37
Monte Vista, Colorado		3,245.46
Total qualified investment as revised		$5,402,139.18
(1) Tentative investment credit 7%		$ 378,149.74
(2) Limitation Based on Amount of Tax		
		Limitation
Tax from page 2	$12,675,341.60	
Less:	(25,000.00)	$ 25,000.00
Excess: Times 25%	$12,650,341.00	3,162,585.40
Limitation based on amount of tax		$3,187,585.40
Allowable investment credit lesser of (1) or (2) above		$ 378,149.74

Rule 50 Computation

STATEMENT OF ACCOUNT	SCHEDULE NUMBER 1	REFERENCE SYMBOLS CC:DEN-TC:RJS:-RDD:ct
NAME AND ADDRESS Adolph Coors Co. Golden, Colorado	DOCKET NUMBER 3179-66	KIND OF TAX Income
	TAXABLE YEAR ENDED	

	12-31-62	12-31-63	12-31-64
REVISED LIABILITY	$9,893,248.18	$10,318,772.28	$12,297,191.86
ASSESSED (*Disclosed by return*):			
DOCUMENT LOCATOR NO.	9,909,682.20	10,440,343.28	12,453,514.44
ADDITIONAL ASSESSMENTS:			
DATE / DOCUMENT LOCATOR NO.			
OVERASSESSMENTS:			
DATE / DOCUMENT LOCATOR NO.			
TOTAL (NET) ASSESSMENTS	9,909,682.20	10,440,343.28	12,453,514.44
Deficiency in Assessment (Overassessment)	$ (16,434.02)	$ (121,571.00)	$ (156,322.58)
REVISED LIABILITY	9,893,248.18	10,318,772.28	12,297,191.86
PAYMENTS (*Dates*)			
1962: 9-18-62	2,000,000.00		
12-14-62	2,000,000.00		
1963: 9-18-63		2,500,000.00	
12-18-63		2,500,000.00	
1964: 3-16-64		2,720,171.64	
4-15-64			103,420.00
6-11-64			103,420.00
9-14-64			2,585,500.00
12-14-64			2,585,500.00
3-15-65			3,537,837.22
6-14-65			3,537,837.22
1963: 3-15-63	2,954,841.10		
6-12-64		2,720,171.64	
LESS REFUNDS (*Dates*)			
TOTAL (NET) PAYMENTS	9,909,682.20	10,440,343.28	12,453,514.44
Deficiency in Payment (Overpayment)	$ (16,434.02)	$(121,571.00)	$(156,322.58)

TAXABLE YEAR ENDED	IR CODE REFERENCE: SECTION	IR CODE REFERENCE: YEAR	DATE RETURN FILED	DATE AGREEMENT EXECUTED	STATUTE EXTENDED TO	DATE DEFICIENCY NOTICE MAILED	DATE CLAIM FILED	AMOUNT OF CLAIM
12-31-62	6512 6511	1954	3-15-63	None	—	3-14-66	None	—
12-31-63	6512 6511	1954	3-16-64	None	—	3-14-66	None	—
12-31-64	6512 6511	1954	3-15-65	None	—	3-14-66	None	—

U.S. TREASURY DEPARTMENT - INTERNAL REVENUE SERVICE — FORM 3623 (7-63)

APPENDIX C

TAX COURT OF THE UNITED STATES

ADOLPH COORS CO.,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Docket No. 3179-66

DECISION

Pursuant to the opinion of the Court filed November 7, 1968, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is an overpayment in income tax for the taxable year 1962 in the amount of $16,434.02, which amount was paid on June 14, 1963, and for which amount a claim for refund could have been filed under the provisions of section 6511(b)(2) of the Internal Revenue Code of 1954, on March 14, 1966, the date of the mailing of the notice of deficiency;

That there is an overpayment in income tax for the taxable year 1963 in the amount of $121,571.00, which amount was paid on June 12, 1964, and for which amount a claim for refund could have been filed under the provisions of section 6511(b)(2) of the Internal Revenue Code of 1954, on March 14, 1966, the date of the mailing of the notice of deficiency; and

That there is an overpayment in income tax for the taxable year 1964 in the amount of $156,322.58, which amount was paid on June 14, 1965, and for which amount a claim for refund could have been filed under the provisions of section 6511(b)(2) of the Internal Revenue Code of 1954, on March 14, 1966, the date of the mailing of the notice of deficiency.

(Signed) J. E. MURDOCK
Judge.

Entered: January 23, 1969

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

/s/ GENE W. REARDON
Counsel for Petitioner
/s/ RICHARD M. HAHN—ELL

RICHARD M. HAHN
Acting Chief Counsel
Internal Revenue Service

APPENDIX D

368

60 T. C. NO. 44

UNITED STATES TAX COURT

WILLIAM K. COORS and PHYLLIS E. COORS, ET AL.,[1] Petitioners *v.* COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket Nos.: 2837-69, 2839-69, 2840-69.
Filed June 12, 1973.

Held:

1. Where the Commissioner did not concede the correctness of the company's accounting treatment of its self-constructed assets in abandoning capitalization adjustments in litigation involving the company for prior years, the doctrines of res judicata and collateral estoppel do not apply to the present litigation.

2. The company's method of accounting for its self-constructed assets does not clearly reflect its income on an annual basis and is erroneous for Federal income tax purposes. Costs of its self-constructed assets represent capital expenditures under section 263, I.R.C. 1954.

3. The Commissioner properly changed the company's method of accounting for self-constructed assets, a recurring material item, and made the necessary adjustments under section 481 in 1965, the year of change, to give the company an increased basis in its self-constructed assets on hand as of January 1, 1965.

[1]Proceedings of the following petitioners are consolidated herewith: Joseph Coors and Holly H. Coors, Docket No. 2839-69; and Adolph Coors Company, Docket No. 2840-69.

4. The company is not prejudiced by the Commissioner's inventory adjustments.

5. Land development costs incurred by the company are nondeductible capital expenditures.

6. Paving and fencing costs are partly deductible business expenses and partly nondeductible capital expenditures.

7. The company's duct work, saw room and valve testing room do not qualify as section 38 property for investment credit purposes.

8. The company is not entitled to deduct social club membership dues paid for the personal benefit of two of its principal stockholders and officers because under section 274 and the implementing regulations it has failed to establish that the primary use of each facility was for business purposes. Certain amounts constitute constructive dividend income to the two shareholders.

9. Certain expenditures by the company made for the purpose of influencing legislation are not deductible.

10. Petitioner William K. Coors is entitled to deduct a net loss in 1966 from the rental of an Aspen condominium.

11. The payment of a guarantor obligation by petitioner Joseph Coors in 1965 is deductible as a non-business bad debt.

Gene W. Reardon, for the petitioners.

Marvin T. Scott, for the respondent.

DAWSON, *Judge:*[2] Respondent determined the following deficiencies in the Federal income taxes of petitioners:

[2]Pursuant to a notice of reassignment sent to counsel for all parties, and to which no objections were filed, these cases were reassigned by the Chief Judge on December 13, 1972, from Judge Austin Hoyt to Judge Howard A. Dawson, Jr., for disposition.

Petitioners	Docket No.	Year	Deficiency
William K. Coors and Phyllis E. Coors	2837-69	1966	$ 3,926.00
Joseph Coors and Holly H. Coors	2839-69	1965	7,952.00
		1966	7,803.00
Adolph Coors Co.	2840-69	1966	3,838,154.33
		1966	1,268,786.83

Various concessions have been made by the parties and will be given effect in the Rule 50 computations. The issues remaining for decision are:

1. Whether the doctrines of res judicata and collateral estoppel apply to certain capitalization adjustments made by the respondent.

2. Whether the cost basis of certain self-constructed assets has been understated by the Adolph Coors Company.

3. Whether respondent's adjustments brought about a change in the accounting method for the costs of the company's self-constructed assets.

4. Whether adjustments under section 481, Internal Revenue Code of 1954, are applicable.

5. Whether the inventory adjustments with respect to the company are proper.

6. Whether certain land development costs incurred by the company are deductible business expenses or capital expenditures.

7. Whether certain paving and fencing costs are capital expenditures or deductible business expenses.

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[2]Pursuant to a notice of reassignment sent to counsel for all parties, and to which no objections were filed, these cases were reassigned by the Chief Judge on December 13, 1972, from Judge Austin Hoyt to Judge Howard A. Dawson, Jr., for disposition.

8. Whether certain property qualifies as section 38 property and is eligible for the investment tax credit.

9. Whether membership dues in social clubs paid by the company on behalf of two stockholders are business or personal expenses and whether such amounts constitute dividend income to the shareholders.

10. Whether certain payments made to influence legislation are deductible by the company as business expenses.

11. Whether William K. Coors is entitled to deduct a net loss from the rental of a condominium in Aspen, Colorado, in 1966.

12. Whether the payment by Joseph Coors of a guarantor obligation in 1965 constituted a business or nonbusiness bad debt.

FINDINGS OF FACT

Some of the facts have been stipulated by the parties. The stipulation of facts and exhibits attached thereto are incorporated herein by this reference.

General

William K. Coors and Phyllis E. Coors, petitioners in Docket No. 2837-69, are husband and wife. Their legal residence at the time they filed their petition herein was in Golden, Colorado. Their joint Federal income tax return for the year 1966 was filed with the district director of internal revenue at Denver, Colorado.

Joseph Coors and Holly H. Coors, petitioners in Docket No. 2839-69, are husband and wife. Their legal residence was in Golden, Colorado, when they filed their petition herein. Their joint Federal income tax returns for the years 1965 and 1966 were filed with the district director of internal revenue at Denver, Colorado.

Adolph Coors Company (sometimes referred to herein as either the company or the corporation) petitioner in Docket No. 2840-69, is a Colorado corporation. Its principal place of business as of the date the petition was filed herein was at Golden, Colorado. Its Federal Corporation income tax returns for the years 1965 and 1966 were filed with the district director of internal revenue at Denver, Colorado. The corporation is an accrual basis taxpayer. Its taxable year is the calendar year.

In 1873 a brewery business was started by Adolph Coors, the father of Adolph Coors, Jr. William K. Coors and Joseph Coors are sons of Adolph Coors, Jr. The brewery has been located in its present location at Golden, Colorado, since that date. In 1913 the business was incorporated under the laws of Colorado and the stock of Adolph Coors Company has been held by the Adolph Coors family since incorporation. A substantial amount of the corporation's capital stock is owned either directly or beneficially by William K. Coors and Joseph Coors.

During the years 1965 and 1966 the principal officers of the corporation were: William K. Coors, president and chairman of the board; Joseph Coors, executive vice president; Adolph Coors, Jr., treasurer; and Ray V. Frost, financial vice president and secretary. The executive committee was comprised of these same officers. These officers and Herman F. Coors, now deceased, comprised the board of directors of Adolph Coors Company. Herman F. Coors resided in Arizona.

The principal business of the corporation is the manufacture and sale of beer. The manufactured beer is placed in bottles, cans, and kegs at its Golden, Colorado, manufacturing plant, from where it is shipped either by railroad car or truck and sold to its 180 distributors throughout the 11 Western States of the United States. Adolph Coors Company is a

regional type brewery and limits its market to 11 Western States. It has only one production plant.

Res Judicata and Collateral Estoppel

In its petition herein the company has affirmatively pleaded res judicata and collateral estoppel with respect to the capitalization adjustments for 1965 and 1966, and with respect to the section 481 adjustment for 1965.

In a previous notice of deficiency involving the years 1962, 1963, and 1964 respondent determined that the company should have capitalized certain construction department overhead costs and maintenance and certain costs of engineering department overhead.

In the section of his brief captioned "Questions Presented" filed in Adolph Coors Company, Docket No. 3179-66, the respondent made the following statements:

> Respondent hereby abandons the adjustment made in the statutory notice of deficiency in the amount of $405,567.07 for 1962, $560,942.25 for 1963, and $310,866.81 for 1964 in Docket No. 3179-66. These amounts represented costs of construction overhead and maintenance and costs of engineering department overhead. Respondent also is hereby abandoning adjustments in the amount of $59,009.60 for 1962, $95,931.74 for 1963, and $122,076.56 for 1964. These amounts represent depreciation on construction equipment which respondent determined to be capital expenditures rather than operating expenses. By abandoning these adjustments, the respondent does not concede one way or the other that Adolph Coors Company's accounting treatment for these items is correct. The respondent is merely abandoning any attempt to change Adolph Coors Com-

pany's treatment of these items for the taxable years 1962, 1963, and 1964. These items were referred to at paragraphs 4D and 4G of the petition in Docket No. 3179-66.

In this Court's Memorandum Findings of Fact and Opinion in *Adolph Coors Company*, T. C. Memo. 1968-256, it was stated:

> The Commissioner in his brief *abandons* the disallowances of deductions made in the deficiency notice of $405,567.07 for 1962, $560,942.25 for 1963, and $310,866.81 for 1964 representing corporation costs of construction overhead and maintenance and costs of engineering department overhead. He also *abandons* disallowances of $59,-009.60 for 1962, $95,931.71 for 1963 and $122,-076.56 for 1964 representing depreciation on construction equipment of the corporation. [Emphasis added.]

In the notice of deficiency for the years 1962, 1963 and 1964 the amounts capitalized by the respondent were determined by adding five percent to the company's capitalized construction costs for such overhead. No specific account-by-account analysis was done. The five-percent figure was an admitted estimate. No effort was made in the previous litigation to make either a section 481 adjustment or an inventory adjustment. The respondent did not believe the earlier adjustment rose to the level of a change in accounting methods but rather considered it merely a correction of an error. The present litigation involves a change in accounting methods and a section 481 adjustment.

Capitalization of Overhead

A. *Growth in Demand*

Since the repeal of prohibition in 1934 the company has steadily increased its production and sales. During the period

from 1934 through 1966 sales and production have increased at an average compounded annual rate of 13 percent. The company projected a substantially similar pattern for the subsequent six years including 1972.

Throughout this expansion period the company has increased its productive capacity to meet consumer demand for its product. This capital asset program has been largely, if not entirely, self-constructed. The company has long thought that economies of scale and production would be essential if it were to survive in the highly competitive brewing industry. During the past 20 years the price of Coors beer charged by the company to its distributors has not increased. By 1966 the company ranked tenth in volume of sales among the Nation's brewing companies. It is the largest regional brewery in the Nation.

The company employs numerous engineers who perform the planning, designing, development and architectural work required for its capital additions program.

The capital budgeting decisions involve long lead times. The increase in sales with its concomitant increase in production requirements means that the company is at times working on some 700 different design phases of construction. Each phase must be closely coordinated with production requirements, material procurement and construction scheduling.

The company erects buildings and other needed structures from its internally developed plans. The company also designs and builds much of the machinery and equipment needed in its brewing operations. The company is able to use its own work force and equipment to build these structures. Most maintenance and repair work is done by its own employees. By doing its own building and maintenance the company obtains two advantages: (1) The production of beer is not interrupted and (2) the cost of such construction is reduced. The industry capitalization cost is approximately $40

per barrel of output. Adolph Coors Company is able to obtain its productive capacity at less than half the industry-wide figure.

To finance its capital asset acquisitions the company relies on internally generated funds. The company does not borrow any capital funds. In 1965 the company had noncurrent (those due in more than one year) liabilities of only $643,922.

A 1965 management report noted that plant expansion was proceeding at an ever accelerating pace. The company had reduced its construction activity in 1964 due to cash flow difficulties. The report then stated that "with 400 employees engaged in actual construction, 70 in design engineering and approximately 30 in supporting staff work, 37 percent of our total staff and much of our top level executive effort is directly involved in plant expansion."

During 1965 the company employees were categorized for record keeping purposes in three classes: (1) office, salaried and management, (2) plant and (3) construction. There was a monthly average of 354 person in office, 588 in plant and 300 in construction in Golden, Colorado. For five months during the year about 31 employees were engaged in construction activities in Monte Vista, Colorado. The number of employees engaged in construction rose throughout the year 1965 from 204 in January to 398 in December. The steady increase in this area of activity continued into 1966. For 1966 the company employed each month an average of 515 persons in construction work. In January 1966, there were 416 so employed; and by December 1966 there were 580 persons employed in such work.

For 1966 the monthly average employment in office, salaried and management, totaled 425; plant required an average of 651 persons per month; and construction required 515. The company was growing rapidly, especially on the

production side of its business. The construction activity increased to keep up with demand. During 1965 the company management was of the opinion that this increased construction activity would enable it to work from a base of adequate facilities "for the sales challenge ahead."

There are three major organizational efforts made by the company. The office and administrative staff work supports the line employees — those who actually produce the finished product; and the other support group involves the construction efforts of an average of over 400 persons. These individuals are employed by the company because of a long-standing policy of self-sufficiency and increased output at a constant sales price.

B. *Accounting Practices and Procedures*

The company has, for cost accounting purposes, 45 separate departments. There is no separate department for the construction activities.

Because of the nature of its product, the company's accounting system has been organized and adapted to a full cost absorption process costing system.

In accounting for self-constructed assets the company capitalizes only certain indirect costs. Indirect costs are not allocated to fixed assets. The company engineers, when working on a capital asset, have their salaries capitalized into the cost of the asset. Engineering department expenses which go through the cost absorption system are not allocated to a fixed asset account. They are treated as expenses by the company and are written off without being reflected either in inventory or in cost of goods sold.

In its chart of accounts the company closes garage costs into truck operating cost. This cost is then allocated to departments on the basis of usage determined by time cards kept for each vehicle. Certain of these costs are then allocated

to fixed assets. Although some of the plant management, personnel and occupancy expenses are distributed to various accounting departments, these costs are not allocated to fixed assets.

Some costs incurred are charged to one of 45 departments. From there they are further allocated to certain subaccounts for cost accounting purposes. At yearend these costs are then regrouped in order to comport with the reporting requirements of the company's Federal income tax return.

According to Ray Frost, the financial vice president, the company-wide effort is concerned with the production of beer. All efforts are directed to such end. The "construction group" of Coors numbered 12 when Frost began working for the company in 1926. In those days the crew was called "Elmer Johnson's Gang." It was their job to build and maintain the company's property. The company now has a maintenance crew doing the day-to-day work of keeping the plant operating efficiently. Major repair jobs as well as construction work are performed by the construction personnel. During the years 1965 and 1966 the construction crew engaged in repair and maintenance work 17.8 percent of their time. In computing his allocations to capital assets, the respondent adjusted the charges incurred by the construction group to reflect this factor.

The construction personnel, when engaged in repair work, would have their time and materials charged to various subledger repair accounts in the department involved.

As one of its 45 accounts the company has an Occupancy account, number 0502. To this account was charged the departmental expenses of the construction effort. From the Occupancy account these charges are then distributed among 14 different departments. A part of the charges to this account are thus reflected in cost of goods sold. The balance of these

expenses are treated as general selling and administrative expenses. No part thereof is allocated to fixed asset accounts.

The total amounts charged by the company to the Occupancy subledger during 1965 and 1966 were $1,901,353 and $2,399,936, respectively. Respondent broke these accounts down and, as a result, capitalized and added to income $886,729.29 for 1965 and $1,346,851.34 for 1966. For 1965 the respondent capitalized 46.6 percent of the amounts charged to Occupancy. For 1966 he determined 56.1 percent of these charges to be capital in nature.

The following table shows the adjustments made by respondent:

Account	1965 Gross Adjustment	1965 Deductible as Repair	1965 Amount Capitalized	1966 Gross Adjustment	1966 Deductible as Repair	1966 Amount
(a) Occupancy-Direct Labor	$ 89,952.37	$ 15,993.53	$ 73,958.84	$ 99,055.90	$ 8,617.86	$ 90,438.04
(b) Occupancy-Supervision	63,406.55	11,273.68	52,132.87	133,096.79	11,579.42	121,517.37
(c) Occupancy-S/W for Repair	234,095.27	41,622.14	192,473.13	212,771.23	18,511.10	194,260.13
(d) Occupancy-Matl for Repair	124,523.28	20,724.62	95,836.82*	187,372.64	15,640.22	164,132.42*
(e) Occupancy-Supplies Exp.	227,952.92	40,530.03	187,422.89	370,566.41	32,239.28	338,327.13
(f) Occupancy-General	7,585.80	1,348.76	6,237.04	8,331.76	724.86	7,606.90
(g) Occupancy-Rent	5,334.33	948.44	4,385.89	9,213.21	801.55	8,411.66
(h) Occupancy-Group Ins.	12,304.74	2,187.78	10,116.96	10,569.72	919.57	9,650.15
(i) Occupancy-Comp. Ins.	72.55	12.90	59.65	2,452.42	213.36	2,239.06
(j) Occupancy-Pers. Dept. Costs	10,318.68	1,834.66	8,484.02	11,258.24	979.47	10,278.77
(k) Occupancy-Plant Mgt. and Research	15,406.02	2,739.19	12,666.83	16,520.61	1,437.29	15,083.32
(l) Occupancy-Truck Costs	120,466.33	21,418.91	99,047.42	215,241.90	18,726.05	196,515.85
(m) Occupancy-Retirement Plan Costs	80,269.54**	14,271.92	65,997.62**	97,395.92	8,473.45	88,922.47**
(n) Occupancy-Depreciation, Bldgs.	18,359.47	3,264.31	15,095.16	20,943.81	1,822.11	19,121.70
(o) Occupancy-Depreciation, M&E	76,397.65	13,583.50	62,814.15	88,002.60	7,656.23	80,346.37
Totals	$1,086,445.50	$191,754.37	$886,729.29	$1,482,793.16	$128,341.82	$1,346,851.34

*Adjusted to reflect concessions made by the parties.

**Conceded by respondent in toto.

The charges to "Occupancy-Direct Labor" that reflected the cost of those support personnel not of the skilled craftsman class engaged in construction activities were withdrawn and capitalized. These individuals work on any given job as directed. They are supportive of the skilled labor employed by the company.

A further charge to this account involved storeroom labor who spent one-half of their working hours in support of the construction department.

During 1965 this account was charged with $191,597.09. Of this, $89,952.37 was construction related. Reduced by the "repair percentage" amount of $15,993.53, the balance ($73,958.84) was capitalized. For 1966 this same procedure resulted in the capitalization of $90,438.04.

The "Occupancy-Supervision" amount was adjusted for salaries paid construction supervisors. The bulk of the salaries paid construction supervisors is capitalized with respect to the capital asset then being constructed. Any salary paid to these supervisors for time not actually spent on site is charged to the Occupancy account. Such non-onsite payments include sick leave, vacation pay, jury duty and the like.

There are certain construction supervisors whose function does not include onsite supervision. The supervisors in central scheduling or in the sheet metal shop do not work on a particular job. The salaries paid to these persons is charged to the Occupancy account and deducted. Respondent reduced this by the standard repair percentage of 17.78 and capitalized the balance.

The account "Occupancy-Salaries and Wages for Repair" was charged with vacation and holiday pay for foremen, repair work on construction department machinery and indirect support activities for the construction effort. To reflect the indirect support activities respondent reduced the gross adjustment by 10 percent in addition to the standard repair per-

centage. For 1965 the amount capitalized was $192,473.13 of the $458,073.53 charged to the account. For 1966 the adjustment totaled $194,260.13 of $470,686.25 so charged.

The charge to "Occupancy-Repair Materials" was adjusted to reflect materials purchased to maintain tools and equipment used in the construction work. This adjustment totaled $95,836.82 for 1965 and $164,132.42 for 1966. The Supplies Expense subledger in Occupancy was reduced by $187,-422.89 for 1965 and $338,327.13 for 1966. The respondent arrived at these adjustments not by an item-by-item examination of all supply material purchased for these two years. A random sample was used. All vendor invoices for February 1966 were analyzed. Each vendor supplying more than $500 charged to this account in 1965 and $1,000 in 1966 was listed. Of the $276,516.67 charged to this account in 1965, $243,762.67 worth of supplies were procured from vendors doing $500 or more in business with the company. The $1,000 or above class of vendors supplied $361,229.97 of the $422,396.69 charged to this account in 1966.

In 1965 the respondent charged 80 percent of the supplies to construction and 20 percent to occupancy. The 1965 repair allocation of 17.78 percent was then applied to arrive at the 1965 capitalization figure.

For 1966 the construction effort consumed 84 percent of the supplies charged to this account, while occupancy utilized the remaining 16 percent.

To arrive at the capitalization ratio the respondent determined that, if over one-half of the dollar amount of the invoice was delivered to "construction receiving," then the entire dollar amount was allocated to construction. If over one-half of the dollar amount of the invoice was delivered to general stores, then one-half was allocated to construction and one-half to occupancy.

In arriving at the net adjustment for 1966 the respondent used as a repair allocation 8.70 percent, reducing the gross adjustment of $370,566.41 to $338,327.13.

The account "Occupancy-Material for Repair" was analyzed in the same manner as supplies expense. The cost of those materials procured primarily for the purpose of maintaining construction equipment was capitalized after a repair allocation was made. In 1965 the adjustment was $95,836.-82; for 1966 it was $164,132.42. Both of these amounts were adjusted to reflect concessions made with respect to residence repairs.

The minor adjustment to "Occupancy-General Expenses" resulted from the capitalization of janitorial services contracted outside the company. These services were rendered exclusively to the construction group.

The minor adjustment of "Occupancy-Rent" represented rental payments for various tools and equipment used in construction. After being reduced by the repair allocation, the balance was capitalized.

Respondent adjusted four nonoccupancy accounts during these two years. These were:

Adjustment	Amount Capitalized	
	1965	1966
Group Insurance	$57,753.34	$ 76,014.21
Plant Mgmt. & Research	71,135.15	116,001.57
Personnel Department	46,597.27	81,290.99
Compensation Insurance	—	17,471.77

These costs are allocated quarterly to various departments on the basis of a ratio of the salaries and wages of the particular department receiving the allocation to the total wages of all departments receiving the allocation.

A portion of the payroll costs of employees working on capital asset projects is capitalized by the company. The per-

centage is developed by dividing the salaries and wages of the particular department by the total wages of all departments receiving the allocation. This figure is then applied to the cost group being allocated. These costs are then distributed to various accounting departments in the brewery, to occupancy and finally to "Payroll Taxes, Capital Accounts."

The same percentage figure showing capitalized salaries is also allocated every quarter to Group Insurance Costs, Compensation Insurance Costs, Personnel Department Costs and Plant Management and Research Costs. These are then charged to a profit and loss account, "Payroll Taxes, Capital Accounts." The amount in this account was taken as a deduction by the company.

Respondent capitalized these claimed deductions dollar for dollar. No repair allocation adjustment was made.

In the Occupancy accounts the company maintains the following subaccounts:

a) Occupancy-Group Insurance Costs
b) Occupancy-Compensation Insurance Costs
c) Occupancy-Personnel Department Costs
d) Occupancy-Plant Management and Research Costs

A portion of the costs of these four groupings is allocated quarterly to the four occupancy accounts bearing the same title. To arrive at the gross capitalization adjustment of the accounts the respondent used the same wage and salary figures used by the company. After being reduced by the repair percentage allocation, the balance in these accounts was capitalized.

The company maintains a Garage Cost subledger as well as a Truck Operating Cost subledger. Garage costs are all closed into truck operating costs quarterly.

During 1965 and 1966 a portion of these costs were allocated to capital assets. In 1965 truck operating costs totaled $539,565.77 of which $153,717.44 was charged to occupancy. In 1966 of $823,865.46 truck operating costs the sum of $268,614.96 was charged to occupancy.

Here again the respondent arrived at his allocation on the basis of a statistical sampling procedure. The analysis of activity showed 82.59 percent of the expense to be attributable to construction, 6.10 percent to occupancy and 11.31 percent was unidentified. The 11.31 percent was not capitalized. Only the 82.59 percent was capitalized. After a repair allocation was applied, the balance was capitalized and disallowed as a current expense.

For 1965 the respondent adjusted the account — "Occupancy-Depreciation, Buildings" with respect to construction property, such as the shops and other out buildings. The depreciation claimed, reduced by the repair allocation, was disallowed as a deduction and capitalized. This was $15,-095.16 in 1965 and $19,121.70 in 1966.

The company charges, either directly or by means of an allocation, depreciation to the separate accounting departments. Depreciation is allocated on a time card basis during which machinery and equipment are actually utilized on a particular capital project. When equipment is idle depreciation on equipment acquired prior to 1965 is charged to an idle equipment account. Depreciation on idle equipment acquired after 1965 is charged to "Occupancy-Machinery and Equipment."

The gross charges to these accounts were reduced by the repair allocation. The balances were disallowed as current expenses and capitalized. With respect to the nonoccupancy account, "Depreciation-Idle Equipment," the amounts disallowed are $25,966.81 for 1965 and $9,853.96 for 1966.

With respect to the account "Occupancy-Depreciation, Machinery and Equipment," the respondent determined that the standard repair allocation $62,814.15 in 1965 was improperly deducted as an expense. For 1966 the improper deduction was found to be $80,346.37. These amounts were capitalized by respondent.

The company maintains a Purchasing Department charged with the responsibility for all purchases for the company. During 1965 the monthly average employment level in the department was 12. In 1966 it rose to 24. The purchasing department maintains several employees on a full-time basis in the construction group in order to expedite their material requisitions. No part of the purchasing department costs is capitalized. They are expensed in full.

The purchasing department was split into two divisions. The efforts of about one-half of the purchasing department employees not physically located in construction related to securing materials needed for the construction of capital assets. Sixty percent of the department's total effort was found to be related to the procurement of construction material. Reduced by the repair allocation, this resulted in the disallowance in 1965 of $82,205.07 as an expense and $160,396.91 in 1966. These amounts were capitalized.

During 1965 and 1966 the monthly average number of employees working in the engineering department was 52 and 70 respectively.

Each engineer and draftsman keeps a time slip to record time spent on each project during the day. These charges are periodically allocated to capital assets under construction.

Engineering costs and construction costs are treated substantially the same. The difference lies in the treatment of overhead costs. Those attributable to the engineering department are so charged. The various occupancy accounts are charged with construction overhead.

All engineering supplies and materials are currently deducted. No part thereof is allocated to fixed assets.

The costs incurred in research and development by the company are currently deducted.

In his analysis of the time cards, respondent found engineering time devoted to repairs as well as to research and development. For 1965, 29.06 percent was found; for 1966 it was 31.19 percent. These percentages were applied to the adjusted engineering department costs to reduce the adjustment to "repairs and other" costs. For 1965 and 1966 the respective amounts of engineering department costs capitalized were $122,779.99 and $157,389.02.

Certain construction workers' labor costs were charged to repairs in the accounting department in which new construction was in progress. These costs included the cost of scaffolding, tool room runners, project rework and site clean up.

No repair allocation was made with respect to the following labor costs:

Department	Capitalized	
	1965	1966
Steam Building	$ 26,416.54	$ 49,667.05
Barley Malting	25,867.58	42,075.71
Beer Bottling	97,155.63	145,308.35
Brewing and Cellars	55,032.70	36,074.58
Totals	$204,472.45	$273,125.69

The amounts allocated to capital construction were further allocated by respondent to individual assets, thus increasing the basis in such assets.

For 1965 and 1966 additional investment credits of $26,-150.79 and $40,140.22, respectively, were allowed by virtue of such capitalization.

The adjustments in capitalization charges resulted in an increase of $531,217.67 in allowable depreciation for the

year 1965. This resulted in a corresponding decrease in 1965 taxable income.

For 1966 the increase in allowable depreciation was $511,-977.38 with a similar decrease in taxable income.

Change in Method of Accounting or Treatment of a Material Item and Section 481 Adjustment

The company's practice of deducting in part as current expense and including in part in cost of goods sold a portion of the direct costs of new capital construction, and all of the indirect or overhead costs of new capital construction, does not clearly reflect income.

The disallowance by respondent of a major portion of the construction department and the engineering department indirect or overhead costs, and the capitalization thereof, constitutes a change in method of accounting or a change in the treatment of a material item within the meaning of sections 446 and 481(a) of the Internal Revenue Code of 1954.

Respondent's method of computation should be applied in determining the company's additional basis in self-constructed assets on hand January 1, 1965.

Respondent's method of computing the section 481 adjustment is reasonable and substantially accurate.

Inventory Adjustments

Respondent adjusted the company's inventory accounts as follows:

Inventory Grouping	Net Adjustments 1965	1966
Inventory of Malt	$ 66,615.51	$ 5,707.64
Inventory in Cellars	127,989.43	84,879.57
Denver Inventories	242.07	26.86
Packages in Bottle House	3,067.49	(807.05)
Totals	$197,914.50	$89,807.02

The adjustments reduced the valuation of the inventory and to that extent reduced taxable income in an amount equal to the adjustment.

The 1966 opening and closing inventories were both adjusted.

Land Development Costs

Respondent determined that certain amounts claimed as expenses by the company and consequently deducted in full in the year incurred were actually a portion of site development costs. Respondent determined that these expenditures were properly includable in the basis of the land. The amounts at issue are:

Cost Grouping	Amount 1965	1966
Relocation of 32nd Ave.	$ 26,681.63	$129,810.33
East Springs Earth Fill		40,621.06
Straightening Clear Creek		12,255.54

Adolph Coors Company is as self-contained as it is possible to be. The company attempts to be vertically integrated throughout its manufacturing process. It obtains Rocky Mountain spring water from wells drilled by it. It purchases hops from Bavaria, rice from California and barley from Colorado. The seed to grow the barley, a most important ingredient to its product, is supplied to certain Colorado farmers by the company. Barley thus grown, which meets its specifications, is purchased. The company has enjoyed considerable success and is one of the ten largest breweries in the country. It has achieved this status in spite of its regional markets and limited number of suppliers.

As a part of its drive for vertical integration, the company determined that it needed a plant to make its own aluminum beer cans to which it affixed its own labels.

The company's Report of Management to its shareholders for the year 1965 states:

> The decision in late 1964 to erect a plant to make 11 oz. aluminum cans required much engineering study. The scope of the plant was increased to include facilities for 15 oz. and 12 oz. cans in addition to the 11 oz. package. In resolving the question of plant location, we ended up with a grand-scale industrial land development project involving some 100 acres of Clear Creek Valley land known to us as the East Springs area. Involved is the relocation of over a mile of state highway and several irrigation ditches and the straightening and re-channeling of Clear Creek. Involved also are 1,500,000 yards of land fill. With additional land parcels either presently acquired or in the mill, the initial 100 acre industrial site can be ultimately expanded to 800 acres which should be ample for the all time needs of our company.

The same management report noted that the "land involved, being almost entirely Clear Creek alluvium, is highly valuable land containing about $25,000 per acre of sand and gravel at today's prices." Predicting a critical shortage of the material in the near future, the company was confident that its value would further increase.

The company was being forced by market demand to operate at full capacity. The company was engaged in substantial capital improvement efforts. A 1966 Management Report noted that the engineering and construction departments were faced with a need to upgrade facilities and to simultaneously add "somewhere in the neighborhood of 500,000 barrels per year of additional brewing capacity."

The company was constantly faced with the need to acquire land upon which to expand its productive capacity to

meet demand. It hoped to achieve parity by 1967. To the east of the company's main plants lay the East Springs area. Through this area of rocks and boulders ran numerous irrigation ditches dependent for their water upon Clear Creek. A public road also ran through this area further segmenting it. Clear Creek itself was an irregular freshet giving rise to a perennial flood threat. This possibility of flooding necessitated the construction of various protective dikes and levees designed to protect existing plant and equipment. As then constituted this area was unsuitable for building.

The company recognized the potential usefulness of this area, as reflected in the minutes of an Executive Committee meeting held March 17, 1965, in which the following was reported:

> Chairman reviewed preliminary talk about locating the can plant east of our plant in the Clear Creek Valley, generally in the area of the land purchased from Val and Henry Blatter, just north of 32nd Avenue. The site could be filled up to about 7′ under the 32nd Avenue level, the Lee Stewart and Eskins Ditch could be tubed and put alongside the road and make a fine area. It would be quite a job as the bottles and machinery now in the area would have to be taken out, the eastern part of the area which we had previously partly filled would have to be picked up, large rocks and concrete broken up, put back and compacted with more dirt being brought in to bring the area level up. After discussing the committee approved this area for the can plant.

Through the East Springs area ran at least one mile of 32nd Avenue. In order to optimize the usefulness of the "grand-scale industrial land development project," this road had to be relocated to the south. The relocation was to serve two

purposes: (1) The bisection of the project would be reduced and (2) the fill from the redeployment excavation could be utilized to raise the level of the East Springs area. Work on both tasks began in August 1965.

Since 32nd Avenue was a public road the company was required to make a request to the Board of County Commissioners before moving ahead. At an Executive Meeting held June 22, 1965, the company's minutes show the following discussion:

> Chairman presented a proposed change of 32nd Avenue east of plant on contour map showing it staying south of the Agricultural Ditch coming back into present road just east of Twin Spruce Subdivision. He stated that in taking dirt for the fill from the new aluminum can plant they would be working in this area and would be doing part of the necessary work on the road relocation which would leave the area as a good site. After discussion it was approved by the committee. It was felt that it should be presented to the County Commissioners to see if they would approve.

The regular meeting of the County Commissioners held on August 30, 1965, reflects in its minutes a request by the company, through its attorney, to be allowed to straighten West 32nd Avenue. The work proceeded apace. The preparatory work, base work, culverts, irrigation ditch relocation was done by the company. The county paved the road segment itself. On October 31, 1966, old 32nd Avenue was vacated by the county and title assumed by the company, and new 32nd Avenue was dedicated by the company to the county.

The total amount spent on this project by the company was $156,491.96. This enabled the company to proceed with its plans.

In order to make the area useful as an industrial site the company incurred substantial costs during 1966 in hauling dirt and fill to the area. This was done in order to raise the level of the land surrounding Clear Creek. This fill was obtained from the site of the work on new 32nd Avenue. The breakdown of the expenses shows the relative importance of the haulage. The complete cost was as follows:

Purchases	$ 64.61
Equipment Depreciation	11,571.00
Salaries and Wages	2,809.55
Truck Operating Costs	26,175.90
Total	$40,621.06

In the general area of the site of the new aluminum can plant nearly 660,000 cubic yards of fill were utilized. This raised the ground elevation at this point by 30 feet.

While the East Springs land fill operation and the relocation of 32nd Avenue were proceeding, the company was also engaged in straightening Clear Creek. During 1966 they spent $12,255.54 to do this. The channel of the creek was relocated and widened. In some areas the creek was moved approximately 1,000 feet in order to straighten its course and define its flow. Portions of the banks of the creek were raised and diked.

The entire effort of moving 32nd Avenue, filling in the East Springs area and straightening Clear Creek was a part of a long-range development project. This project revitalized the area and made it possible to build additional productive capacity. The bettering of the land has had a beneficial effect on its value.

Paving and Fencing Costs

In his notice of deficiency the respondent determined:

> The amount of $7,961.84 claimed as expense for material for repairs is not allowed because it per-

tains to asphalt paving which is a capital expenditure. Of this amount, $7,617.84 is allowed as a depreciation asset and $344.00 pertains to residence furnished to Adolph Coors, Jr., which is disallowed as an expense deduction or as a depreciable asset. Therefore, your taxable income is increased $7,961.84.

On brief the respondent conceded the amount of $344 spent to repair certain asphalt driveways appurtenant to the residence of Adolph Coors, Jr. This left the $7,617.84 at issue. The expenditures were:

Vendor	Amount
Table Mountain, Inc.	$ 872.24
Asphalt Paving Co.	3,745.60
Lifetime Fence Co.	3,000.00
Total	$7,617.84

Of the $7,961.84 claimed as an expense for 1965, the petitioner was able to produce invoices totaling $7,665.34.

The Table Mountain, Inc., invoices covered road base gravel material purchased during 1965. The invoices from Asphalt Paving Co., covered asphalt repair work between the cellars and Clear Creek as well as the application of a slurry seal on the employees' parking lot. The invoices from Lifetime Fence Co., covered repairs and replacement of various fences on the factory site.[3]

For 1966 the company claimed a deduction of $7,600 as repair expenses with respect to paving and fences. At the trial the petitioner orally conceded that paving costs in the amount of $4,248.76 should properly be capitalized. The remaining $3,351.23 expense deduction is poorly documented.

In disallowing the claimed expenses for paving and fencing costs, respondent determined that the assets had a useful

[3]The testimony adduced at trial from Mr. Field indicated the possession of invoices from Lifetime Fence Co., of $2,379.36. The difference between this and the respondent's capitalization of $3,000 was not explained.

life of eight years and should have been depreciated on that basis.

Investment Credits

A. *Duct Work*

During 1965 and 1966 the company placed into service sheet metal duct work in the basement and the fourth floor of its bottle packaging building. In 1965 the petitioner spent $3,344.77 on such installation. In 1966 the petitioner further expended $13,656.62. The item here involved is approximately three to five feet thick, six to ten feet wide and 100 feet in length. The duct work is part of an air handling system involving a louvered system mounted on the roof of the bottle packaging building. There is included in this system an air plenum with a large filter installation. A water spray system and blowers complete the system. The duct work involved is attached to the package building by means of steel angle braces.

The equipment filters the air prior to diffusion in the area of distribution. The building is not completely serviced by this unit. The function of this air handling equipment is to remove foreign matter from the air before it is released into the packaging plant.

Although the air is cooled by means of a water spray it is not an air cooling system as such. The equipment is not utilized to heat this building. The heating function is performed by an independent and entirely separate system.

B. *Saw Room*

During 1965 and 1966 the company expended $6,900 and $500, respectively, in constructing a saw room. The investment credit was affirmatively claimed in the petition. The saw room is on a mezzanine floor in the bottle packaging building. It is a solid constructed room of approximately 30 feet by 40 feet. It has a door and a window with a load bear-

ing roof. The room contains saws used to remove the tops from boxes containing returned beer bottles. The dust is removed by means of ventilating ducts. The bottles are then shunted off to a cleaning process before being refilled. The room encloses a conveyer belt system. The cartons enter the room via the conveyer through an opening in one wall and following the process exit through the other end of a continuous feed process.

The investment credit was claimed for the expenditure involved in the construction of the room but not for the equipment contained therein.

C. *Valve Testing Room*

In 1966 the company spent $4,870 in order to construct a valve repair and maintenance workshop. This room in the bottle packing plant is capable of other uses.

The room itself is 30 by 20 feet in size. It is of masonry construction. The walls of this room are permanently affixed to the building. It has windows and doors. The roof of this room can be utilized as a storage area. A stairway on the outside of the room provides access to the rooftop storage area.

Social Club Dues

During 1965 and 1966 the company paid the annual dues at various social clubs used by two of the principal officers of the company, namely, William K. Coors and Joseph Coors. These club dues are as follows:

Club	Dues 1965	Dues 1966	Officer
Lakewood Country Club	$ 484.00	$ 372.00	Joseph Coors
Denver Country Club	600.00	600.00	Joseph Coors
Rolling Hills Club	420.00	420.00	Joseph Coors
Hiwan Golf Club	240.00	240.00	William K. Coors
University Club	333.60	343.20	William K. Coors
Denver Club	360.00	360.00	William K. Coors
Denver Country Club	600.00	600.00	William K. Coors
Garden of the Gods Club	105.00	100.00	William K. Coors
Totals	$3,142.60	$3,035.20	

During these years numerous other charges were incurred by William K. Coors and Joseph Coors. Such charges over the two years in question amounted to $4,558.10. Of these the corporation paid $948.12 (20.8 percent) and the individuals paid $3,609.98 (79.2 percent). Respondent did not disallow the entertainment expenses paid by the company. He did, however, disallow the claimed deductions totaling $6,177.80 for 1965 and 1966 dues paid.

In arriving at a breakdown of the charges as to those paid by the company and those paid by the individuals the respondent resorted to the handwritten notations made on the statements by the individual users.

During 1965 and 1966 Joseph Coors' business and personal use of the clubs, by days of use, as taken from the monthly statements was:

	Days of Use			
	1965		1966	
Social Club	Personal	Business	Personal	Business
Rolling Hills Club	7	0	1	0
Lakewood Country Club	5	0	4	0
Denver Country Club	20	2	23	1

During 1965 and 1966 William K. Coors' business and personal use of the clubs, by days of use, as taken from the monthly statements was:

	Days in Use			
	1965		1966	
Social Club[4]	Personal	Business	Personal	Business
University Club	1	0	2	0
Denver Club	23	0	19	0
Denver Country Club	38	1	54	0

Thus, out of a total 201 days-in-use, only four days may be attributed to business use and the remaining 197 days are attributed to personal use.

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[4]The Hiwan Golf Club monthly statements do not reflect usage by day. During 1965 and 1966 the company paid only the dues while William K. Coors paid $786.74 and $953.39, respectively, for personal expenses incurred there.

Respondent further determined that Joseph Coors realized dividend income of $1,504 for 1965 and $1,592 for 1966; and that William K. Coors realized dividend income in 1966 of $1,643.

These social club memberships have been maintained by the company in the names of the key officers for many years. Except for 1965 and 1966, the respondent has not questioned the deductibility of such payments. Several of the clubs permit corporate memberships which allow several named members from a single company to utilize the club. Other clubs refuse to permit this, and for business functions a named individual must be in attendance.

The company does business with all these clubs in that there are business functions scheduled there. Business guests are lodged there and make use of the facilities. Similarly all of the clubs serve the company's product — Coors beer.

Payments Made to Influence Legislation

For each of the years 1965 and 1966 the company claimed a deduction for "dues and subscriptions." Certain of these payments were determined by respondent to have been made to organizations whose purpose and function it was and is to influence legislation. The organizations and amounts paid were:

Organization	Amount 1965	1966
National Right to Work Committee	$100.00	
Colorado Tax Equality Committee	250.00	
Committee for Constructive Government	100.00	$ 100.00
Colorado Plan for Apportionment		1,000.00
Committee for Nonpolitical Selection		250.00
Totals	$450.00	$1,350.00

Aspen Condominum

William K. Coors acquired a condominium apartment in Aspen, Colorado, in late October 1965. During 1965 the apartment was not rented. William Coors and his wife spent some time at the apartment during the last quarter of 1965 readying the apartment for rental.

William Coors had a cost basis in the apartment and its furnishing of $41,897.

The apartment was operated under a rental agreement with a property management firm in Aspen which undertook to rent the apartment for Mr. Coors. In addition to a management fee, the agent was to receive 20 percent of any rental income.

It was standard practice for William to receive, at some point during the summer, a calendar on which he was to block off the dates on which he proposed to use the apartment. The remainder of the time was available for rental. During 1966 William blocked out one week at Christmas and one week in the spring. For the balance of the year the agency attempted to rent the apartment. During 1966 the apartment was rented for approximately 21 days. For this period of rental William Coors received $788.

During 1966 William Coors reported a net loss from the condominium of $2,492. This was determined by adding depreciation ($2,039) to other deductions ($1,241) and deducting therefrom the rental income ($788). The respondent disallowed the net loss deduction of $2,492 asserting only that William Coors had not established that he was "entitled to such a deduction."

Bad Debt

Sometime prior to 1965 Joseph Coors was interested in the perfection of an audio-visual device intended to permit communication between persons of different languages. The

idea was related to him by a prep school companion. His interest aroused, Joseph Coors sought out and obtained the services of Paul Flury,[5] an engineer then working for Coors Porcelain Company. To enable Mr. Flury to proceed in the development work for this device, Joseph Coors guaranteed a loan made by the Golden State Bank to Paul Flury.

In 1964 Joseph Coors paid $1,253.83 in legal expenses incident to research and development of a patent of a visual and audio language interpreter. This claimed deduction was disallowed. In other litigation in this Court with the year 1964 at issue Joseph conceded that $450 paid in connection with the patent to an attorney to establish a corporation was not deductible. This patent was the first in which Joseph had any financial interest. The balance of the deduction was disallowed because there was insufficient proof to show that Joseph was regularly engaged in any business in which the amount paid to a patent lawyer would constitute an ordinary and necessary business expense.

Because of personal problems Mr. Flury terminated his employment with Coors Porcelain Company and severed his relationship with Interpretor Corporation. Mr. Flury has disappeared and no one has heard from him since 1965. During 1965 Joseph was called upon by the bank to repay the loan. He paid $2,167 to the bank under his guarantor obligation. On his 1965 Federal income tax return this sum was deducted as a business bad debt.

OPINION

1. *Res Judicata and Collateral Estoppel*

The Adolph Coors Company has raised the defenses of res judicata and collateral estoppel with respect to respondent's capitalization of overhead costs. The company argues that

[5]The spelling of this individual's name varies in all briefs and the transcript.

(1) the same issue was in controversy between the parties for the years 1962, 1963, and 1964; and (2) that this Court finally determined the capitalization of overhead issue adverse to the respondent and therefore the issue is no longer properly before us.

The company states that our "redetermination of respondent's capitalized overhead determination in the old case for the immediate three prior years constitutes a sufficient judgment for res judicata purposes for the instant two following years." *United States* v. *Utah Idaho Sugar Company,* 15 A.F.T.R. 1037 (D.C. Utah, 1934), is cited. That case appears to have been one in which a complaint by the Utah Idaho Sugar Company, lodged in the United States Court of Claims, was dismissed upon agreement of certain "law officers" of the United States and counsel for the company. Later other United States "law officers" instituted an action in the United States District Court for the District of Utah seeking relief from the agreement. The District Court dismissed the action summarily. The same parties dismissed the cause of action in the Court of Claims and then one party sought relief from the effect of such dismissal in another forum. Labeling its reasons for dismissal "res judicata," the District Court dismissed the action, noting that the proper way for the Government to obtain relief was to directly attack the settlement and compromise. Whether or not such an attack would succeed in view of the Court's previous finding of "res judicata" need not concern us here. We simply do not find the case controlling in these circumstances.

The capitalization of certain overhead for 1962, 1963, and 1964 was not settled and compromised by the parties. Respondent is not seeking in the present case a redetermination of those years with respect to the capitalization issue. The years involved in the present case (1965 and 1966) are different and distinct from the previous case. In the prior case

no findings, either mediate or ultimate, were made by the Court with respect to such issue.

The doctrine of res judicata applies where issues that were or could have been determined in an earlier suit are presented anew to the Court. If such action is taken by one party to attempt to relitigate such issues, the idea of repose and consideration of judicial economy operate to bar further review. The necessity of finality applies in the area of tax law as much as in other areas of the law. But the prior case did not result in any determination of the capitalization issue. The "significance of what a court says it decides is controlled by the issues that were open for decision." *Angel* v. *Bullington,* 330 U.S. 183, 187 (1947). The capitalization issue was merely abandoned by respondent for the three years then at issue. The Court did not reach that question in *Adolph Coors Company,* T.C. Memo. 1968-256.

The doctrine of collateral estoppel applies where matters are actually litigated and determined in the first cause of action. This principal is stated in the Restatement on Judgments, section 68, as follows:

> A judgment on one cause of action is not conclusive in a subsequent action on a different cause of action as to questions of fact not actually litigated and determined in the first action.

The Supreme Court of the United States has said, in the area of consent judgments, that the spirit of justice requires the doctrine to be limited to cases where there was "an adjudication on the merits." *United States* v. *International Building Co.,* 345 U.S. 502, 506 (1953). *Lawlor* v. *National Screen Service Corp.,* 349 U.S. 322, 326 (1955), teaches that the doctrine should apply only as to "issues actually litigated and determined in the prior suit."

The argument that this Court would have determined the capitalization issue, except for the abandonment, is tenuous

at best. It fails to consider the fact that each taxable period is a separate and distinct cause of action. The case of *Heasley* v. *United States,* 348 F.2d 40 (C.A. 8, 1965), cited by the petitioner, is not apposite. There the Heasley family prevented from relitigating a previous tax lien judgment entered against them under the guise of a suit for damages against the United States. The Court of Appeals noted at p. 42:

> If anything is settled in the law, it is that the parties to a lawsuit and their privies are precluded from relitigating issues conclusively settled by a former judgment. [Citations omitted.]

Clearly the capitalization issue here involved has not yet been conclusively determined by any court of competent jurisdiction.

That portion of the doctrine of res judicata barring later litigation of that which could have been raised in the former proceeding must be viewed in the light of the principle set forth in *Burnet* v. *Sanford & Brooks Co.,* 282 U.S. 359 (1931), that each taxable year is separate and distinct. The respondent correctly points out that this doctrine does not override certain ameliorative provisions of the Code which seek to bridge the gap between separate years in order to avoid possible unintended and harsh results.

The historical and practical differences between res judicata and collateral estoppel were discussed by this Court in *John W. Amos,* 43 T.C. 50, 53-54 (1964), affirmed 360 F.2d 358 (C.A. 4, 1965), as follows:

> Collateral estoppel, or estoppel by judgment as it is often referred to, is an adjunct of the ancient judicial doctrine of res judicata.[3] While the two bear much in common, having derived from a singular purpose, they are by no means the same. Res judicata applies only to the *same* cause of action arising between the same parties. Its effect,

where there has been a decision on the merits in a cause of action between two parties, is to preclude future litigation between those parties or persons claiming through them, "not only as to every matter which was offered and received to sustain or defeat the claim or demand, but as to any other admissible matter which *might* have been offered for that purpose" in the prior proceeding. *Cromwell* v. *County of Sac,* 94 U.S. 351, 352 (1876). Collateral estoppel, on the other hand, applies in a *different* cause of action. It operates as an estoppel, not as to matters which might have been litigated and determined, but "only as to those matters in issue or points controverted, upon the determination of which the finding or verdict [in the prior case] was rendered." *Cromwell* v. *County of Sac, supra.* [Footnote omitted.]

Where "the cause of action involved in the second proceeding is not swallowed by the judgment in the prior suit, the parties are free to litigate points which were not at issue in the first proceeding, even though such points might have been tendered and decided at that time." *Commissioner* v. *Sunnen,* 333 U.S. 591, 598 (1948).

Collateral estoppel will not bar an issue that was neither pleaded nor considered even if it could have been dealt with. *Muriel Dodge Neeman,* 26 T.C. 864 (1956), affirmed 255 F.2d 841 (C.A. 2, 1958). The application of collateral estoppel requires that the issue be considered by a court. If the court expressly refuses to discuss an issue, later litigation on the issue is not barred. See *Kimbell-Diamond Milling Co.,* 14 T.C. 74 (1950), affirmed without consideration of this point, 187 F.2d 718 (1951). The other end of the spectrum from issues not pleaded and consequently not barred involves findings not necessary to the determination of an issue. Here

again collateral estoppel will not apply. *Moore* v. *United States,* 360 F.2d 353 (C.A. 4, 1965), affirmed on this point, 235 F.Supp. 387 (W.D. Va. 1964); *Laughlin* v. *Commissioner,* 21 A.F.T.R.2d 869 (C.A.D.C. 1967), affirming per curiam a Memorandum Opinion of this Court; and *Piper* v. *United States,* 392 F.2d 462 (C.A. 5, 1968).

In our opinion the interests of justice would not be properly served if the facts relating to the capatilization issue were to be deemed conclusively established on the basis of the prior case. See *The Evergreens* v. *Nunan,* 141 F.2d 927, 929 (C.A. 2, 1944), certiorari denied 323 U.S. 720 (1944), where the Court said:

> [I]t often works very harshly inexorably to make a fact decided in the first suit conclusively establish even a fact "ultimate" in the second. The stake in the first suit may have been too small to justify great trouble and expense in its prosecution or defense; and the chance that a fact decided in it, even though necessary to its result, may later become important between the parties may have been extremely remote. It is altogether right that the judgment shall forever put an end to the first cause of action; but it is not plain that it is always fair that every fact * * * decided in it shall be conclusively established between the parties in all future suits, just because the decision was necessary to the result.

That is the case here. The capitalization issue was abandoned by respondent; no findings were made by the Court with regard to the issue; and it was not necessary to the result reached. To these considerations it should also be pointed out that we are dealing with a new taxable period and the principle that the respondent is not forever bound by a previous determination made in a statutory notice of deficiency.

Just as the doctrine of equitable estoppel does not bar the Commissioner from correcting an error in his interpretation of the law, *Automobile Club* v. *Commissioner*, 353 U.S. 180, 183 (1957); *John S. Neri*, 54 T.C. 767 (1970), the abandonment of an issue with respect to certain tax years does not bar the Commissioner from raising the issue again in later years.

Accordingly, we conclude that the doctrines of res judicata and collateral estoppel do not apply to this litigation.

2. *Capitalization of Overhead Expenses*

In his notice of deficiency the respondent made adjustments to the company's taxable income for 1965 with the following explanation:

> Deductions claimed for expenses in connection with your construction department in the amount of $1,497,639.37, as shown in Exhibit A attached, are not allowed because it is determined that such amounts represent capital expenditures rather than operating expenses. Accordingly, your taxable income is increased in the amount of $1,497,639.37.

The notice of deficiency also covered the year 1966. The adjustment and explanation for that year stated:

> Deductions claimed for expenses in connection with your construction department in the amount of $2,238,395.46, as shown in Exhibit D attached, are not allowed because it is determined that such amounts represent capital expenditures rather than operating expenses. Accordingly, your taxable income is increased in the amount of $2,238,395.46.

It is respondent's view that these expenditures are not properly expenses currently deductible and should not be included in cost of goods sold. He contends that they are capital expenditures properly added to the basis of the assets to which the costs are attributable.

The company accounts for its product — beer — using a full cost absorption system. Capital assets are charged with the direct costs involved in placing them in service.

A flow chart of the company's accounting program shows 45 separate accounting departments. For each department there are numerous subledgers which contain the varied accounts necessary to attribute the costs of operating a particular department.

Examination of this chart reveals that the first 36 accounts pertain to the production of beer. These accounts begin with Plant Management progressing from Truck Operating to Water Treatment to Barley Malting, to Brewing and Cellars to Sewage Disposal. These costs all affect inventory and cost of goods sold.

The amounts of direct cost, depreciation and payroll are derived from the source documents and charged directly to the various departments. Other amounts are allocated to the various departments using varied formulas. Plant Management and Personnel costs are allocated on a payroll basis. Truck Operating Cost is allocated on the basis of usage as shown on time cards. Plant Protection and Greenhouse costs are allocated directly to Occupancy which in turn is allocated to 14 departments on the basis of net value of depreciable assets as reported for property tax purposes. Costs involved for such items as Water Treatment, Refrigeration, Sewage Plant are allocated to certain departments on the basis of fixed percentages. Others such as Laboratory costs are allocated on a fluctuating percentage. Engineering, Traffic, and Purchasing are added to administrative which is expensed currently.

Among the 45 accounts there is not a construction department account. The expenditures incurred in this area of the

company's activities are charged to various accounts in the Occupancy subledger. The costs gathered in Occupancy are either directly expensed, assigned to inventory or reflected in cost of goods sold. No part of the Occupancy account is allocated to fixed assets. These departmental costs are allocated directly to the department and indirectly with respect to various self-constructed assets.

The construction personnel employed by the company were not expected to perform repair and maintenance work as a regular part of their duties. Separate maintenance teams were employed to keep the brewery operative. The construction personnel would be detailed to only the major repair projects. To reflect this effort a repair allocation was made in order to remove from the capitalization figures the effect of repair work performed by construction personnel.

The direct costs incurred in the Engineering department are allocated to the fixed assets to which they relate. The overhead costs of that department are not allocated to fixed assets.

The Purchasing department overhead costs are not allocated to production accounts or to asset accounts. The amounts involved have been expensed.

Respondent argues that the company is utilizing an improper method of accounting in dealing with the actual costs of self-constructed assets. The full cost absorption system utilized by the company to account for the production costs reflects direct, indirect, fixed and variable costs. With this method and practice of accounting the respondent fully agrees. The difference between a full cost absorption system and a direct costing approach is best seen by viewing what a direct costing system omits. The direct costing approach omits fixed cost from its consideration. The omission of any one of the following costs — direct, indirect or variable — necessarily results in something less than a direct costing system.

The omission of a required element of cost from a given asset and the concomitant expensing of the item will understate the cost basis of assets for depreciation purposes. The failure to properly treat overhead expenses has a twofold effect on the company's accounting. It tends to overstate the cost of goods sold in a given year. This understates income as well as the cost basis of any assets to which costs are not properly allocated. Where this cost basis is improperly reduced by means of a current deduction, income is improperly reflected. It follows that any distortion in the cost basis of capital assets, normally recoverable by way of depreciation, will affect income in future years.

Section 263 (a)(1) of the Code provides, in pertinent part, that no deduction shall be allowed for "any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate." Section 1.263(a)-2(a), Income Tax Regs., provides that "the cost of acquisition, construction, or erection of buildings, machinery and equipment, furniture and fixtures, and similar property having a useful life substantially beyond the taxable year" are examples of capital expenditures.

Where a method of accounting used by a taxpayer "does not clearly reflect income, the computation of taxable income shall be made under such method as, in the opinion of the Secretary or his delegate, does clearly reflect income." See section 446(b).

In the instant case it is a fact that the company has followed its accounting practices for many years. However, the Commissioner may, in the exercise of his discretion, order such a change. The broad powers available to the Commissioner in determining the correctness of a method of accounting have been noted often. See *Automobile Club of Michigan* v. *Commissioner*, 353 U.S. 180, 189-190 (1957); *Schlude* v. *Commissioner*, 372 U.S. 128 (1963); *S. Garber, Inc.*, 51 T.C. 733, 735-736 (1969). The burden is upon the taxpayer

to prove the correctness of his chosen method of accounting. Conclusionary statements that the method was correct, in long use and often approved, are not sufficient to carry that burden.

We need not decide whether a chosen method of accounting is the *best* method available or whether it is the most widely used method. To do this would put us in the position of attempting to establish "recognized methods of accounting" for various segments of business. We think it is preferable to allow the line of "clearly reflecting income" to be pricked out by adverse parties with vital interests at stake. Our decisions and those of other courts will then provide the means of determining acceptable methods. We recognize, as respondent does, that no "uniform method of accounting can be prescribed for all taxpayers." Section 1.446-1(a)(2), Income Tax Regs. This approach necessarily places the burden on the parties to articulate their respective positions with the ultimate burden of persuasion resting with the taxpayer.

The company's argument that its method of treating these overhead costs had been long utilized and tacitly approved can be answered by saying that consistency does not make it right. A failure to clearly reflect income over many years cannot be justified on the grounds of tenure. See *Photo-Sonics, Inc.*, 42 T.C. 926 (1964), affirmed 357 F.2d 656 (C.A. 9, 1966) ("an erroneous method does not become acceptable solely upon the consistent use over an extended period of time."); *Dearborn Gage Co.*, 48 T.C. 190 (1967); *Sam W. Emerson Co.*, 37 T.C. 1063 (1962); *Geometric Stamping Co.*, 26 T.C. 301 (1956); *All-Steel Equipment, Inc.*, 54 T.C. 1749 (1970), affirmed on this issue 467 F.2d 1184 (C.A. 7, 1972).

The company relies heavily on cases in which the respondent has successfully required the use of full cost absorption accounting. By asserting the fiction that there is no construc-

tion department and that respondent has agreed that the accounting method chosen to reflect the cost of its product (beer) does clearly reflect income, the company reaches the conclusion that the full cost absorption method is being correctly used. The fallacy in this position is the assertion that there is no construction department. The scope of this effort, the costs and skills involved, management references to a "construction department," the company policy of self-constructed assets so as to not impede the production of beer, the existence of a separate maintenance unit and the functional realities of the situation lead us to the conclusion that construction was as much a way of life at Adolph Coors Company as the production of beer. A failure to have an accounting department for the construction activity will not hide its existence.

The company's construction department is highly diversified. It is largely self-sufficient and self-contained. The machinery and equipment used in its construction effort is owned by it. Expansion of its facilities is accomplished by personnel employed in its construction department. At times the number of employees whose efforts were devoted to construction exceeded the number of employees whose efforts were devoted to the production of beer. In essence, the company's energies are devoted to two activities. One is the production and sale of beer. The other is the construction of new plant and equipment to enable it to produce and sell more beer. General support is needed for the production of new assets probably to a greater extent than general support is needed for the production of beer.

The company cites and relies heavily upon *Fort Howard Paper Co.*, 49 T.C. 275 (1967). Unfortunately for the company, the crucial facts of this case simply do not fit the mold or rationale of *Fort Howard*. The facts of that case are stated in our opinion (49 T.C. at pages 282 and 285) as follows:

At least as far back as 1939, petitioner followed a policy of using repair and maintenance personnel during their spare time in the construction, renovation, and repair of fixed assets used by petitioner in its manufacturing operations. At no time were such personnel diverted from regular repair and maintenance activities to work on such self-constructed assets.

At all times the size of petitioner's repair and maintenance staff was determined exclusively by its need for the continuous operation of its regular producing equipment. No special tools or machinery were acquired for use by such personnel in their activities on self-constructed assets. Respondent does not contend that petitioner maintained a larger than necessary repair and maintenance staff as a cover for its self-construction activities, and, indeed, there is no evidence in the record before us to support any such conclusion.

> At this point, it is useful to recall the salient facts regarding petitioner's policy with respect to self-constructed assets. Petitioner did not in any way augment its personnel to construct these assets. It relied entirely on its repair and maintenance staff to do this work and then only during "slack" or "idle" time, so that the normal flow of production activities was in no way affected. Thus, petitioner's policy achieved a "double duty" objective. In a very real sense, petitioner killed two birds with one stone. There is nothing in the record before us which indicates that there was any increase in overhead costs which could be directly identified with the self-constructed assets.

In *Fort Howard,* the Commissioner took the position that the paper company was employing the prime cost method

of accounting for its self-constructed assets and that the full absorption cost method was the proper method. The paper company contended that it was employing the incremental cost method of accounting and that such a method was acceptable for commercial accounting purposes.

Since this Court decided in *Fort Howard* that the costs which the Commissioner sought to capitalize were largely costs that would have been incurred in any event, the method of accounting was undoubtedly a consideration secondary to the factual distinction. In *Fort Howard,* the crucial distinction is the "idle time" factor. If an employee is in any event essential to the current production effort, but that employee has spare time and to conserve against the waste of his time he is placed in the construction of an asset during slack periods which in no way interferes with his maintenance functions, then there is no increment or variance in costs above what would have been incurred in any event had not the construction taken place. That is the rationale of this Court in *Fort Howard*. Those facts are clearly distinguishable from the employees in the construction department and the engineering department at Adolph Coors Company, and the costs of running that massive construction effort. Here, by contrast, we are concerned with the increment to which costs vary because of in-house construction over what such costs would have been had the new assets been acquired by contract from outside sources.

Since *Fort Howard* largely involved labor costs which would have been incurred in any event, there no doubt were little, if any, variable costs involved. Hence, the difference between prime costing and incremental costing would seemingly have been insignificant as applied to the facts of that case in reaching a dollar result. That is quite different in the case of Adolph Coors Company since essentially all of the costs involved, other than direct costs, are variable costs. To a limited extent this case involves what would be viewed as

fixed costs or period costs, if we were concerned with the beer production effort alone. However, by using the company's own figures, such as those costs allocated to the expense account "Payroll Taxes, Capital Accounts," it becomes readily apparent that the costs of certain "fixed overhead" type activities vary considerably when in-house construction of such massive proportion is undertaken and, conversely, such costs are not nearly so "fixed" in amounts as they would have been had these activities been concerned with beer production alone.

Unlike *Fort Howard,* there would not appear to be any major differences between an application of the "incremental cost" method and the "full cost absorption" method in the instant case since the costs involved here, other than direct costs, are primarily variable costs with which incremental costing is concerned and not nonvariable or fixed costs, the addition of which is the progression from incremental costing to full absorption costing. The important step involved in the instant case is between prime costing, which the company's system is intended to accommodate for self-constructed assets, and incremental costing.

Finally, an application of the accounting principles enunciated by the authorities cited in *Fort Howard, supra* at 285, to the facts of this case clearly reveals that the method used by the company in accounting for the cost of its self-constructed assets is not accepted for purposes of commercial accounting.

We think respondent has not abused his discretion in requiring a change in the company's method of accounting for self-constructed assets. As our previous discussion indicates, the method of accounting used by the company fails in two major respects to clearly reflect income and is therefore erroneous. First, it causes a distortion of current income by causing cost of goods sold to be overstated in the current year and, in a corresponding amount, causes the costs of self-constructed assets to be understated. Secondly, it causes a

distortion of the current year's income to the extent that capital construction costs are deducted as current expenses. The cumulative effect is to take as current expense or as a part of cost of goods sold amounts which should be capitalized and recovered through depreciation in later years. This will cause the income in future years not to be clearly reflected. Moreover, from the standpoint of commercial accounting, the practice of capitalizing only certain direct costs of new capital construction is not an acceptable method of accounting in the unique factual setting of this case, and is unacceptable for Federal income tax purposes. See and compare *Ben Perlmutter,* 44 T.C. 382 (1965), affirmed 373 F.2d 45 (C.A. 10, 1967).

In our opinion there is no justification in either accounting theory or in Federal tax law for the company's failure to absorb costs in assets to which the costs unquestionably relate. Had Adolph Coors Company procured its capital additions by contract from an outside source, included in the cost it would have incurred would be all of the costs we are concerned with here plus a profit to the builder. Obviously, the acquiring of capital additions, whether by purchase or by self-construction, is appropriate, if not vital, to the company's continued expansion, but this fact does not cause the cost of these capital additions to be deductible in the year acquired. And it is unrealistic to suggest that by in-house construction the company can, for Federal tax purposes, properly expense all costs of capital construction other than certain direct costs. This would not only offend the provisions of section 263 but would also distort annual accounting and income for Federal tax purposes. See and compare *Southern Natural Gas Company* v. *United States,* 412 F.2d 1222, 1265 (Ct. Cls. 1969).

The company has made a rather general, hit-and-run attack on respondent's determination as being arbitrary and capricious. If the respondent's determination is arbitrary, it

is clear that the presumption of correctness disappears. It is our view, however, that the company's evidence herein does not establish arbitrariness. At most, it raises suspicion, and that has been dispelled by respondent. Although the determination may not "rise to the dignity of glittering perfection," it nonetheless has a rational basis and is therefore not arbitrary.

3. *Section 481 Adjustments*

Section 481(a) of the Code provides that where taxable income for any taxable year is computed by means of a method different from that utilized to compute taxable income for a preceding taxable year then —

> (2) there shall be taken into account those adjustments which are determined to be necessary solely by reason of the change in order to prevent amounts from being duplicated or omitted, except there shall not be taken into account any adjustment in respect to any taxable year to which this section does not apply unless the adjustment is attributable to a change in the method of accounting initiated by the taxpayer.

Section 1.481-1(a)(1), Income Tax Regs., amplifies the meaning of "a change in method of accounting" in the following terms:

> A change in method of accounting to which section 481 applies includes a change in the over-all method of accounting for gross income or deductions, or a change in the treatment of a material item.

Section 1.446-1(e)(2)(ii)(a), Income Tax Regs., likewise provides that a change in the method of accounting includes both a change in the overall method of accounting for gross income or deductions and "a change in the treatment of a material item."

Respondent argues that the company has consistently failed to add to the cost basis of various self-constructed assets certain costs incurred in placing those assets into use. This failure in accounting methodology and practice has resulted in the deductibility of substantial amounts of money in the year incurred.

For the purposes of section 481, "method of accounting" includes, at least, a change in the treatment of a recurring material item. *Shepherd Construction Co.*, 51 T.C. 890, 898 (1969); *Fruehauf Trailer Co.*, 42 T.C. 83, 104 (1964), affirmed 356 F.2d 975 (C.A. 6, 1966), certiorari denied 385 U.S. 822; *Electric & Neon, Inc.*, 56 T.C. 1324 (1971). Even if a practice of accounting is erroneous, it may nonetheless be a method of accounting. *Fruehauf Trailer Co., supra.*

In *Peoples Bank and Trust Co.*, 50 T.C. 750, 756 (1968), affirmed 415 F.2d 1341 (C.A. 7, 1969), this Court said:

> The term "method of accounting" includes the accounting treatment of any item. Sec. 1.446-1(a)-(1), Income Tax Regs. The treatment initiated by respondent was a change in the treatment of a material item, thus constituting a change in petitioner's method of accounting. [Citation omitted.]

No argument is made by the company that the item involved is not material. Respondent has asserted a "year of change" increase in taxable income of $7,042,325.93[6] for 1965. The amounts capitalized for the years 1965 and 1966 are $1,497,639.37 and $2,238,395.46, respectively.

Since the respondent initiated this change in method of accounting the adjustment in taxable income made for the "year of change" will include only those years to which the 1954 Internal Revenue Code applies. For the years since 1954 the improperly deducted capital asset costs must be restored.

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[6]This reflects the limitation imposed by section 481(a)(2).

This sum will be added to the basis of the assets and will be subject to depreciation thereafter. Obviously, if the amount of previously deducted costs were only added to the basis of the assets and thereafter recovered under various depreciation methods, a double benefit would accrue to the company. The aversion to a double deduction on the part of respondent is understandable. The statute, however, bars pre-1954 years from the applicability of the adjustment. For those years a possible double deduction exists. This is understood and accepted by respondent. See sections 1.481-1(a)(2), 1.481-1(c)(3), and 1.481-3, Income Tax Regs., *Fruehauf Trailer Co., supra,* to which the respondent has acquiesced.

Respondent has determined that the company incurred $9,580,728.91 in additional capital construction costs during the years 1954 through 1964. From this he has deducted allowable depreciation of $1,700,597.17 to arrive at the additional basis as of January 1, 1965, of $7,880,131.74.

In the pre-1954 years the respondent has determined that additional capital construction costs of $2,067,370.35 were incurred. Pre- and post-1954 depreciation totals $1,328,-916.67, resulting in an additional basis as of January 1, 1964, of $738,453.68.

Section 481(a)(2) bars the addition to income in 1965 of $1,576,259.49 which is computed by subtracting the pre-1954 capital construction costs ($2,067,370.35) that were expensed. This "windfall" must be subtracted from the gross amount capitalized for both pre- and post-1954 ($8,618,-585.42), resulting in the section 481 adjustment of $7,042,-325.93.

The company has argued that the section 481 adjustment is subject to possible error and as such is arbitrary and capricious. We reject this argument.

We conclude that respondent's change of the company's consistent, but erroneous, treatment of a recurring material

item is correct, and that the adjustments made necessary by sections 446 and 481 of the Code were correctly applied in 1965, the year of change.

4. *Inventory Adjustments*

The company asserts that it has been prejudiced by respondent's inventory adjustments. Adjustments to inventory occurred because of respondent's capitalization of that portion of construction costs absorbed in the various inventories. Closing inventory for 1965 was adjusted to exclude therefrom amounts capitalized for that year alone to the extent that such costs were included in closing inventory. The closing inventory for 1965 was carried forward to reflect the correct opening inventory for 1966. Closing inventory for 1966 was adjusted to exclude construction costs included therein to the extent that such costs were capitalized by respondent for the year 1966. The difference between the adjusted opening inventory for 1966 and the adjusted closing inventory for 1966 represents the net cost of goods sold adjustment for 1966. There were no specific adjustments to inventory prior to the adjustments to closing inventory for 1965. However, the failure of respondent to make such adjustments is to his prejudice and not to the prejudice of the company.

Respondent's exclusion of construction costs from inventory reduced the unit cost of inventory units on hand at the close of 1965 and 1966. The reduced unit cost was multiplied by the number of units on hand to arrive at the closing inventory for each year. In computing inventory, the number of units used by respondent is the same as the number of units used by the company in valuing its closing inventory. Only the unit cost of certain inventory groupings was corrected, but the number of units on hand at the close of each year was in no way adjusted.

The adjustments to inventory do not modify the company's full cost absorption method of accounting for inventory.

These adjustments are premised on respondent's position that certain fixed asset costs, as opposed to production costs, were erroneously entered into manufacturing costs. Adjustments to inventory are merely ancillary to an attempt to segregate capital expenditures from production costs.

In connection with the company's cost absorption system, a portion of its capital construction costs were through allocation and reallocation improperly absorbed in cost of goods sold. This causes cost of goods sold to be overstated, resulting in gross profit on sales being understated and ultimately causes taxable income to be understated. However, for practical purposes, it matters not on an annual basis whether the capital costs are included in cost of goods sold or current expense with the exception of the effect these costs have on the various inventories. Other than with respect to inventories, production costs are in effect expensed during the year the inventory is either consumed or sold in much the same manner as nonproduction costs are expensed.

Closing inventory is, in a sense, a deferral of expense to a subsequent accounting period when that inventory is either consumed or sold. This is necessary to properly reflect income on an annual basis. Hence, the ultimate effect of respondent's disallowance and capitalization is to reduce inventories to the extent that capital construction costs were improperly included therein.

The company claims that the respondent erred in not adjusting malt pellet inventory. We note, however, that any adjustment to malt pellet inventory is insignificant because of the small amount on hand at the end of the year coupled with the slight amounts of capital construction costs absorbed in malt pellet inventory.

In these circumstances we conclude that Adolph Coors Company is not prejudiced by respondent's inventory adjustments.

5. *Land Development Costs*

In a period of two years the company expended $209,-368.56 in relocating 32nd Avenue, moving land fill to the East Springs area and straightening a portion of Clear Creek. It deducted the expenses in the years incurred as ordinary and necessary business expenses. Respondent determined that the expenditures are nondeductible and should be added to the company's basis in the land.

The company contends that the expenses constitute "deductible business expenses as reported, rather than capital expenditures." To the contrary, respondent points to section 263(a)(1) which provides that no deduction shall be allowed for "any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate." Respondent asserts that "the expenditures increased the value of the property."

We do not accept as realistic the company's assertion that it was neutral with respect to the relocation of 32nd Avenue. We think the evidence shows the obstacle the road presented to the industrial development plans of the company. The company was constantly pressed to increase its capacity. It enjoyed a rising demand for its product and wished to expand its sales. Whether or not the company made the initial overture to the Board of Supervisors, the minutes of the supervisors indicate that the company presented its plans for such relocation and the supervisors deferred immediate action until their staff was able to prepare studies and contact affected individuals. The road was relocated by the company and, after completion and dedication, the company received title to the land previously utilized by the road.

The cost/benefit analysis that was done with respect to the industrial development in terms of capital expenditures and market penetration must have convinced the company to proceed with its development.

The rechanneling and diking of Clear Creek was an investment in security for the new can plant to be built in the East Springs area. This is to be the industrial area sufficient for "the all time needs of the company." The investment in the stream rerouting and diking must be viewed as a capital item and not a deductible expense.

In its brief the company cites *Converse* v. *Earle*, 43 A.F.-T.R. 1308 (D.C. Ore. 1951). That case held that $9,031.45 spent to build a logging road was an ordinary and necessary business expense and currently deductible. The decision contained no discussion and no authorities were cited. The *Converse* case was later cited and followed by *Regan* v. *United States*, 20 A.F.T.R.2d 5759 (D.C. Ore. 1967). On the appeal of the *Regan* case to the Ninth Circuit the error was rectified. See *United States* v. *Regan*, 410 F.2d 744, 746 (C.A. 9, 1969), certiorari denied 396 U.S. 834 (1969), where the Court of Appeals said:

> Are expenditures for building access roads capital expenses? We think they are * * *. We disapprove of anything in *Converse* and *Watts* which may be contrary to our views herein expressed.

See also *Casey* v. *United States*, 459 F.2d 495, 496 (Ct, Cl. 1972), involving the same partnership as *Regan*. The Court of Claims, in holding that the road expenditures were capital items, said:

> The above Ninth Circuit decision [*United States* v. *Regan, supra*] not only reversed the decision below [*Regan* v. *United States, supra*], but it went further and disapproved anything contrary in *Watts* v. *Erickson*, 10 A.F.T.R.2d 5832 (D.C., Ore., 1962) and *Converse* v. *Earle*, 43 A.F.T.R. 1308 (D.C., Ore., 1951). Plaintiffs herein rely very much on these two cases but *Converse* and *Watts* are no longer the law in the Ninth Circuit.

We hold that the expenditures to shape and mold the land resulted in an improvement in the land itself and must be capitalized.

6. *Paving and Fencing Costs*

This is an often litigated issue in which the line of demarcation between a repair (currently deductible) and a capital expenditure (depreciable) is a fine one.

In *Plainfield-Union Water Co.*, 39 T.C. 333, 338 (1962), this Court indicated that the proper test for distinguishing a repair from a capital expenditure is

> whether the expenditure materially enhances the value, use, life expectancy, strength, or capacity as compared with the status of the asset prior to the condition necessitating the expenditure.

See also *Illinois Merchants Trust Co., Executor*, 4 B.T.A. 103 (1926), where we looked at the purpose for which an expenditure was made. The approach was to distinguish between a repair made to repair or mend and a replacement which connotes a substitution.

The company claims that materials aggregating $6,997.20 for 1965 and $3,351.23 for 1966 were "incidental repairs" which did not prolong the life or add to the value of the roads, the parking lot or the fences. Respondent, on the other hand, contends that the costs for such items are capital expenditures, primarily because the company has not established their deductibility.

For the year 1965 we hold that the $2,420.80 paid to Asphalt Paving Company for the application of slurry seal to the employees' parking lot has all the appearances of a make-do repair and is deductible. The practice of putting a slurry seal — a watery mixture of insoluble matter — on a parking lot is not a replacement of the paving material. It is

a make-do, recurring item. It is at best a cosmetic rehabilitation with no structural value. But all of the other costs, particularly those paid to Lifetime Fence Company ($2,379.36) which were for the replacement of fences and fence posts, are capital expenditures. The same is true for the asphalt paving, which is not merely a repair.

For the year 1966 respondent's capitalization of paving costs is a specific adjustment in the amount of $7,600 pertaining to the amount paid Asphalt Paving Company for the paving of four areas at the brewery. The company's chief accountant testified that $4,248.76 of that amount was for new paving pertaining to four areas at the brewery which amount should be capitalized; but that $3,351.23 was for repairs. He failed to give any indication of the repairs involved. Hence we sustain respondent's adjustment in its entirety.

7. *Investment Credits*

In his notice of deficiency respondent disallowed various items of investment credit. At the time of trial five items for which the credit was claimed had not been resolved. Concessions following the trial have resulted in three items remaining in controversy.

The material facts relating to cost, date of expenditure and useful life are not at issue. The only question is whether the components qualify as "section 38 property" for the years involved.

A. *Duct Work*

It is the duct work described as three to five feet thick, six to ten feet wide and approximately one hundred feet long that is in question.

Section 38 of the Code provides for the allowance as a credit against tax for qualified investments in property. Section 48(a)(1) defines the term "section 38 property" to mean:

> (1) In general. — Except as provided in this subsection, the term 'section 38 property' means —
>
> (A) tangible personal property, or
>
> (B) other tangilbe property (not including a building and its structural components) but only if such property —
>
> (i) is used as an integral part of manufacturing, production, or extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, * * *

The term "tangible personal property" is defined in section 1.48-1(c), Income Tax Regs., as

> any tangible property except land and improvements thereto, such as buildings or other inherently permanent structures (including items which are structural components of such buildings or structures) * * *. Tangible personal property included all property (other than structural components) which is contained in or attached to a building.

Respondent argues that none of the components at issue falls within the definition of "tangible personal property." The regulations permit property (other than a building or its structural components) to qualify as "section 38 property." The requirement for such qualification is that the property be used as an integral part of the manufacturing or production process. Section 1.48-1(d), Income Tax Regs. Respondent agrees that the components are part of the facilities used as an integral part of the company's manufacturing process. It is the parenthetical phrase (other than a building or its structural components) on which respondent focuses. If the items are buildings or structural components thereof, they are excluded from the purview of section 38 property.

Section 1.48-1(e)(2) includes as a "structural component" the duct work associated with a central air-conditioning system. It speaks of an air-conditioning system. The apparatus here involved is just such a conditioning system. The regulation excludes those structural conponents the sole justification of which is the necessity to meet temperature or humidity requirements essential to the processing of foodstuffs.

The testimony of the expert witness for each side was of little value. Each witness stated that the property was or was not section 38 property depending upon his affiliation with the parties. It is our view that the duct work (specifically listed as a structural component) cannot be separated from this category under the exclusion for essential temperature and humidity control apparatus.

B. *Saw Room*

This room is an area within the confines of the bottle packaging plant. It contains apparatus used in removing the tops of cartons carrying reusable bottles. The saw room itself is not within the exclusion contained in section 1.48-1(e) of the regulations which attempts to define buildings and their structural components. This exclusion reads as follows:

> Such term [building] does not include (i) a structure which is essentially an item of machinery or equipment, or (ii) an enclosure which is so closely combined with the machinery or equipment which it supports, houses or serves that it must be replaced, retired, or abandoned contemporaneously with such machinery or equipment, and which is depreciated over the life of such machinery or equipment.

The room itself is not an item of machinery such as a wind tunnel. Nor is it so closely entwined with the cutting machinery that its useful life is mirrored by the useful life of the

equipment it encompasses. We think the saw room is different from the moveable, replaceable room partitions accorded section 38 treatment. *Minot Federal Savings & Loan Association* v. *United States,* 313 F.Supp. 294 (D.C.N.D., 1970), affirmed 435 F.2d 1368 (C.A. 8, 1970). To read the *Minot* case as supporting the view that the "intent of the investment credit statutes was to include all tangible property as qualifying for the credit excepting land and improvements" is clearly wrong.

C. *Valve Testing Room*

This workshop area was provided for the purpose of performing maintenance and repair facilities needed for the valves used in the production of beer. This room obviously provides working space. It is excluded by the terms of the regulations from section 38 status. See section 1.48-1(e)(1), Income Tax Regs.; *Robert E. Catron,* 50 T.C. 306, 312-313 (1968).

Accordingly, we hold that the company's duct work, the saw room and the valve testing room do not qualify as section 38 property and therefore the company is not entitled to the claimed investment credits on such property.

8. *Social Club Dues.*

Respondent disallowed deductions of $3,142.60 in 1965 and $4,442 in 1966 claimed by the company as business expenses. Such disallowance also resulted in a determination that William and Joseph Coors received constructive dividend income.

Throughout these proceeding the company has maintained that the respondent has permitted it to take deductions for club dues for many years. From this tacit approval, the company draws the inference that what has been accepted in the past must be accepted for the present and the future. That is incorrect. It is firmly established that the Commissioner is

not precluded from determining that a taxpayer is not entitled to a deduction in the amount claimed in succeeding taxable years, even though he previously approved a like deduction in an earlier year. See and compare *Dinkins* v. *Commissioner*, 378 F.2d 825 (C.A. 8, 1967); affirming 45 T.C. 593 (1966); *Dixie Furniture Co.* v. *Commissioner*, 390 F.2d 139 (C.A. 8, 1968), affirming a Memorandum Opinion of this Court; and *Estate of Goodall* v. *Commissioner*, 391 F.2d 775, 783 (C.A. 8, 1968). Nor is it correct to assert that the Commissioner's acquiescence in prior tax returns and the treatment of given items thereon will operate as an admission against interest by the respondent. See *Wiles* v. *United States*, 312 F.2d 574 (C.A. 10, 1962). A prior determination cannot serve to relieve a petitioner of his burden of proving error in the Commissioner's present determination. See *Walker* v. *Commissioner*, 362 F.2d 140 (C.A. 7, 1966), affirming a Memorandum Opinion of this Court.

The evidence shows that the company has maintained these various club memberships for many years. The evidence also shows that the respondent has not disallowed all club expenses. The entertainment expenses charged to the company on the basis of the notations made on the statements by the principal-officers were uniformly allowed. Respondent also allowed a deduction for the membership dues of Adolph Coors, Jr., in the Lakewood Country Club.

The company asserts that the clubs sell petitioners' products; the memberships have been maintained for several years; business associates utilize the facilities; and the company holds some business functions there.

The issue is whether the company's payment of annual dues incident to the memberships of its two principal officers in the social clubs is deductible as an ordinary and necessary business expense under section 162 of the Code. More directly involved is section 274 and the implementing regulations

which provide that social club dues are not deductible at all unless the facility is used primarily for business purposes during the taxable year, and that if it is used primarily for business purposes, then only that portion of the membership dues established as being directly related to the active conduct of a business during the year is deductible. Section 274 of the Code sharply limits entertainment expense deductions made after 1962 even though they might otherwise qualify under section 162. See sections 274(a)(1)(B) and 274(d)-(2). Congress made the conscious decision that more shall be required to obtain an entertainment expense deduction than merely asserting that the expenditure was an ordinary and necessary item incurred in the taxpayer's trade or business. See *William F. Sanford*, 50 T.C. 823 (1968), affirmed per curiam 412 F.2d 201 (C.A. 2, 1969), certiorari denied 396 U.S. 841 (1969). Uncorroborated oral testimony is insufficient to entitle one to the deduction. *John L. Ashby*, 50 T.C. 409 (1968); and *Charles A. Bane*, T.C. Memo. 1971 -31, affirmed per curiam, unreported (C.A. 7, 1972). *Cf. LaForge* v. *Commissioner*, 434 F.2d 370 (C.A. 2, 1970), reversing in part and remanding 53 T.C. 41 (1969).

Under section 274(a)(1)(B), as amplified in section 1.274-2(e)(4)(i), Income Tax Regs., it is the actual use of the social club which is determinative as to the primary use test as opposed to either its availability for use or the member's principal purpose in joining the club. Section 1.274-2 (e)(4)(i) further provides that "objective rather than subjective standards will be determinative" of primary use.

Section 1.274-2(e)(4)(i) provides that in determining the nature of each use the factors to be considered include the frequency and duration of use for business purposes as compared with other purposes, and the amount of expenditures incurred during use for business compared with the amount of expenditures incurred during use for other pur-

poses. However, that section goes on to state that no one of the standards is exclusively determinative.

In the case of the three social clubs of which Joseph Coors was a member during 1965 and 1966, an objective application of the evidence to the primary use of the facility test is conclusive of the fact that none of the objective standards provided by section 274 and its implementing regulations is met. Since the primary use requirement has not been satisfied, we think no portion of the social club dues paid by the company on behalf of Joseph Coors during 1965 and 1966 is deductible as an ordinary and necessary business expense to the company during each of those years.

In the case of the five social clubs of which William K. Coors was a member during 1965 and 1966, the evidence supports the fact that, from a standpoint of "the dollar test" and "the times of use test" in arriving at primary use, the University Club and the Denver Club were not primarily used for business purposes during the years 1965 and 1966. The same is true of the Denver Country Club for 1966. Since the primary use requirement has not been satisfied, we think no portion of the dues paid by the company on behalf of William K. Coors is deductible with respect to his University Club and the Denver Club memberships for 1965 and 1966 and his Denver Country Club membership for 1966.

William K. Coors' membership in the Denver Country Club was used one time for business purposes and 38 times for personal purposes during 1965. However, the expenditure for the one occasion of business use is $814.18 and the aggregate of the expenditures in connection with the 38 times of personal use is $359.58. As previously indicated, there is no one particular test that satisfies the primary use requirement to the exclusion of other objective standards. However, where a facility was used 38 times for personal reasons and only one time for business reasons, it is our view that the

primary use of the facility was not for business purposes. Thus, we conclude that this item does not constitute expense deductible by the company during 1965.

The substantiation required by section 274(d)(2) to establish that a facility was used primarily for business purposes is most precise. *Otho B. Ross, Jr.*, T.C. Memo. 1970-110. It specifically requires adequate records or corroborated verbal statements as to use. In the case of William K. Coors' memberships in the Hiwan Golf Club and the Garden of the Gods Club for 1965 and 1966 the substantiation as to use as required by section 274(d)(2) is wholly lacking. Sections 274(a)(1)(B) and 274(d)(2) make the dues expense of these two clubs unavailable as a deduction to the corporation in 1965 and 1966 in the absence of precise proof as to the primary use for business purposes. The company has failed to do this.

We hold that the company has not established that the social clubs here involved were used during 1965 and 1966 primarily for the furtherance of its business. This is an indispensable requirement of section 274(a)(1)(B) if the social club membership dues are to be allowed as an ordinary and necessary business expense. Accordingly, it follows that such amounts are not deductible by the company in 1965 and 1966.

Club dues paid by a corporation for the personal benefit of its shareholders constitute dividend income. *Commissioner* v. *Riss*, 374 F.2d 161, 170 (C.A. 8, 1967). A substantial amount of the stock of Adolph Coors Company is owned either directly or beneficially by William and Joseph Coors. The social club dues at issue here were paid by the company primarily for the *personal* benefit of William Coors, its president, and Joseph Coors, its executive vice president, and as such constitute constructive dividend income to them, as follows:

	1965	1966
William Coors	none	$1,643.00
Joseph Coors	$1,504.00	1,592.00

See *Louis Greenspon,* 23 T.C. 138 (1954), affirmed on this issue 229 F.2d 947 (C.A. 8, 1956); *American Properties, Inc.,* 28 T.C. 1100 (1957), affirmed per curiam 262 F.2d 150 (C.A. 9, 1958); and *Irving Sachs,* 32 T.C. 815, 820 (1959), affirmed 277 F.2d 879 (C.A. 8, 1960).

The company offered no evidence that such amounts were paid for the benefit of William and Joseph Coors in their capacity as employees. Consequently, we are unable to find that the amounts constituted additional compensation to them and were deductible by the company.

9. *Payments Made to Influence Legislation*

For each of the years 1965 and 1966 the company claimed deductions for "dues and subscriptions" paid to certain organizations in the total amounts of $450 and $1,350, respectively. Respondent determined that these were payments to organizations the purpose of which is to influence legislation and for this reason the payments do not constitute ordinary and necessary business expenses. Payments made to influence legislation are not deductible. See section 1.162-20, Income Tax Regs.; *Cammarano* v. *United States,* 358 U.S. 498 (1959).

The company introduced no evidence on this issue. It has failed to carry its burden of proof. We therefore sustain respondent's determination.

10. *Aspen Condominium*

As to this issue, we must decide whether William Coors' condominium at Aspen, Colorado, was held for the production of income within the purview of section 212 of the Code. The petitioners contend that it was so held. Respondent contends that it was not because the petitioners had no profit-seeking motive.

William and Phyllis Coors own a condominium unit in a multiple-unit building located at Aspen. Their cost basis in the condominium and its furnishings is $41,897. On their 1966 income tax return they reported rental income in the total amount of $788. They claimed a deduction for depreciation in the amount of $2,039 and other deductions of $1,241, resulting in a net loss of $2,492.

Petitioners contracted with an Aspen rental agency to rent and manage the apartment in 1966. The agency is paid a substantial fee to care for the apartment and, in addition, receives a commission of 20 percent of the rental proceeds. Each summer the rental agency furnishes the petitioners with an annual occupancy schedule; they block out and reserve a week in the spring and a week in the winter for personal use of the apartment; and the rental agency attempts to rent the apartment for the remainder of the year.

If the "predominant purpose" and use of the property was for recreation, a hobby or some other nonprofit motive, and not to derive income therefrom, then no deductions are allowable. Section 1.212-1(c), Income Tax Regs. In this connection it is well settled that the absence of a profit is not determinative, but the use of the property should be of such a nature that in good faith the taxpayer genuinely expected or intended to make a profit. See *Henry P. White,* 23 T.C. 90, 94 (1954), affirmed 227 F.2d 779 (C.A. 6, 1955); *Margit Sigray Bessenyey,* 45 T.C. 261 (1965), affirmed 379 F.2d 252 (C.A. 2, 1967). The issue is factual, and we find on this record that the petitioners did have a profit-seeking motive and thus held the property for the production of income in 1966. That was the first year of attempted rental and it is understandable that the market was slow. It is significant that it was held out for rental about 95 percent of that year.

We think *Carkhuff* v. *Commissioner,* 425 F.2d 1400 (C.A. 6, 1970), affirming a Memorandum Opinion of this

Court, is distinguishable on its facts. In that case there was substantial use of a Sea Island cottage by the taxpayers during peak rental periods. Under the circumstances the taxpayers failed to prove they had a profit motive.

Accordingly, we hold for the petitioners on this issue. In doing so, we note that the provisions of section 183 and the regulations thereunder do not apply to the year 1966.

11. *Bad Debt*

The facts pertaining to this issue are incomplete, unclear and conflicting. However, it appears that Joseph Coors and two other individuals entered into a venture to perfect and market an audio-visual communication device. One of them (Flury) borrowed money from a bank. Joseph Coors guaranteed the loan. The venture was unsuccessful. Flury defaulted on the bank loan and disappeared. Joseph Coors, as guarantor, paid off the loan of $2,167 in 1965. Respondent determined that the debt was a nonbusiness bad debt instead of a business bad debt, as reported by the petitioner.

Petitioner argues that the payment in discharge of his obligation as a guarantor of the loan constitutes a business bad debt deduction under section 166(f) of the Code.

In order for a bad debt to be deductible under section 166(f) the elements to be satisfied are: (1) The guarantor must not be a corporation; (2) the guaranteed debt must not be that of a corporation; (3) the loan proceeds must be used in the principal debtor's (borrower's) trade or business; and (4) the principal's debt to the lender must be worthless at the time the guarantor makes good on his obligation and pays the lender.

The facts relative to this particular debt show that there was a noncorporate guarantor who guaranteed a noncorporate debt which at repayment was in fact worthless. On brief the respondent questions only "whether the loan proceeds

were used by Flury in *his* trade or business." The issue, as viewed by respondent, is whether or not the borrowed funds were utilized in the borrower's trade or business. He argues that it is the utilization and not the relationship giving rise to the guarantee that determines the tax treatment. Petitioner cites *Axelrod* v. *Commissioner*, 320 F.2d 327 (C.A. 6, 1963), reversing 37 T.C. 1053 (1962), to the effect that it is the "business relationship" that brings the debt within the provisions of section 166(f).

The exact nature of the business engaged in by Paul Flury and the nature of his relationship with either Joseph Coors or Interpretor Corporation is not clear. In our opinion in *Adolph Coors Co.*, T.C. Memo. 1968-256, we observed that "Flury worked for Joseph Coors in some way." During the present trial Joseph Coors testified that at the time he enlisted the aid of Flury, he (Flury) "was working for our company, Coors Porcelain Company at that time." From this testimony it appears that Flury was an employee of Coors Porcelain Company at the time of his disappearance and that his involvement with the development of the language machine was an incidental activity outside of his fulltime employment at Coors Porcelain Company. At another place in the record Joseph Coors indicated that his association with Flury was something akin to a joint venture. Interpretor Corporation was apparently formed in 1964. Whether Flury was a part-time employee of that corporation is not clear. But we know that the patent on the language machine was granted to Flury and assigned by Flury to the Interpretor Corporation. Joseph Coors held stock in the Interpretor Corporation.

The facts in *Axelrod* v. *Commissioner, supra,* are in all vital respects different from the unclear and conflicting facts herein; therefore, we regard *Axelrod* as distinguishable. A going business was involved there and the loan proceeds were used to allow that going business to continue. By contrast, the

"business relationship" here has not been shown. In view of the confused and irreconcilable testimony regarding this matter, the business, if any, of Flury (the borrower) is not established. The language machine was never perfected and there was no going business to continue.

Even if Flury was at least engaged in the trade or business of developing the patent on the language machine, the petitioner has failed to prove that the borrowed money was used in the business. Such evidence could have been produced by Joseph Coors. Nothing in this record shows a proximate link between the loan and its use in any trade or business.

In these circumstances we conclude that Joseph Coors is only entitled to a nonbusiness bad debt deduction for the payment of his guarantor obligation.

To reflect the various concessions made by the parties and our conclusions with respect to the disputed issues,

Decisions will be entered under Rule 50.

UNITED STATES TAX COURT
WASHINGTON

WILLIAM K. COORS AND PHYLLIS E. COORS, ET AL., *Petitioners,* v. COMMISSIONER OF INTERNAL REVENUE, *Respondent.*	Docket Nos. 2837-69, 2839-69, 2840-69

ORDER

On June 12, 1973, the Court filed its Findings of Fact and Opinion [60 T.C. No. 44] in these cases. For cause appearing to the Court, it is

ORDERED:

1. That on page 36, line 8, of the Findings of Fact the word "be" is stricken and the words "have been made to" are substituted in lieu thereof.

2. That on page 75, lines 19 and 20, of the Opinion the following sentence is stricken: "Oral testimony alone is insufficient to entitle one to the deduction." In lieu thereof the following sentence is substituted: "Uncorroborated oral testimony is insufficient to entitle one to the deduction." At the end of line 22, page 75, of the Opinion the following citation is added: Cf. *LaForge* v. *Commissioner,* 434 F.2d 370 (C.A. 2, 1970), reversing in part and remanding 53 T.C. 41 (1969).

3. That on page 78, lines 3 and 4, of the Opinion the following sentence is stricken: "It specifically requires records to corroborate verbal statements as to use." There is

substituted in lieu thereof the following sentence: "It specifically requires adequate records or corroborated verbal statements as to use."

In all other respects the Findings and Opinion remain unchanged.

HOWARD A. DAWSON, JR.
Howard A. Dawson, Jr.
Judge

Dated: Washington, D.C.
June 14, 1973

APPENDIX E

United States Court of Appeals
TENTH CIRCUIT

JULY, 1975, TERM

ADOLPH COORS COMPANY
Petitioner-Appellant,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent-Appellee.

No. 74-1468

ON APPEAL FROM THE DECISION OF THE
UNITED STATES TAX COURT
(No. 2840-69)

Gene W. Reardon, Denver, Colorado, for Petitioner-Appellant.

Robert A. Bernstein, Tax Division (Scott P. Crampton, Assistant Attorney General, Gilbert E. Andrews and Jonathan S. Cohen, Tax Division, on the brief), Washington, D.C., for Respondent-Appellee.

Before HILL, SETH and BARRETT, United States Circuit Judges.

HILL, Circuit Judge.

This is an appeal by Adolph Coors Company (taxpayer) from a United States Tax Court decision sustaining the Commissioner of Internal Revenue's determination of federal income tax deficiencies for the years 1965 and 1966 in the amounts of $3,838,154.33 and $1,268,786,83, respectively.

The relevant facts may be summarized as follows. Taxpayer is a Colorado corporation engaged in the production and sale of beer. It uses its own equipment and employees in the construction of improvements and additions to its capital facilities. Taxpayer employed 398 construction personnel (37% of its work force) in 1965 and 580 construction personnel in 1966. Their major tasks consisted of erecting buildings and other improvements and constructing much of the machinery and equipment used in taxpayer's brewing operations.

Although taxpayer maintains this large construction crew, and although it maintains forty-five separate departments for accounting purposes, it has never created a separate department to account for its construction activities. Under its system of accounting the direct costs of construction activities are allocated to various departments and charged to capital assets. However, the indirect or overhead costs of these construction activities are not similarly capitalized. Instead, these expenditures are allocated to an occupancy (general overhead) account. From this account they are reallocated among various production and administrative departments. Production costs are reflected as costs of goods (beer) sold and administrative costs are reflected as ordinary and necessary business expenses. The result is that these construction-related costs are fully deducted by taxpayer in the taxable year in which such costs are incurred.

In 1966 the Internal Revenue Service (IRS) assessed federal income tax deficiencies against taxpayer for the years 1962, 1963 and 1964. These deficiencies were based upon a determination by the IRS that (1) taxpayer had unreasonably accumulated its earnings; (2) certain items of taxpayer's property did not qualify for investment credit purposes under 26 U.S.C. § 38; (3) various deductions relating to two of taxpayer's residences were improper, and (4) indirect costs attributable to the construction of new plant facilities,

amounts taxpayer had deducted as operating expenses, represented capital expenditures.

Taxpayer filed a petition in the Tax Court seeking a redetermination of the asserted deficiencies. Following a trial at which all the deficiencies were litigated, the IRS filed a brief which stated, in part:

> Respondent hereby abandons the adjustment made in the statutory notice of deficiency in the amount of $405,567.70 for 1962, $560,942.25 for 1963, and $310,866.81 for 1964. . . . These amounts represented costs of construction overhead and maintenance and costs of engineering department overhead. Respondent also is hereby abandoning adjustments in the amount of $59,009.60 for 1962, $95,931.74 for 1963, and $122,076.56 for 1964. These amounts represent depreciation on construction equipment which respondent determined to be capital expenditures rather than operating expenses. By abandoning these adjustments, the respondent does not concede one way or the other that Adolph Coors Company's accounting treatment for these items is correct. The respondent is merely abandoning any attempt to change Adolph Coors Company's treatment of these items for the taxable years 1962, 1963 and 1964.

The subsequent opinion of the Tax Court, which disposed of the other issues in favor of the taxpayer, stated:

> The Commissioner in his brief abandons the disallowances of deductions made in the deficiency notice . . . representing corporation costs of construction overhead and maintenance and costs of engineering department overhead.

On March 13, 1969, the IRS again assessed deficiencies against the taxpayer, this time for the year 1965 and 1966 in

the amount of $3,838,154.33 and $1,268,786.83, respectively. The IRS disallowed, inter alia, deductions as expenses of the overhead costs of construction on the grounds such amounts represented capital expenditures. It also determined that the capitalization of overhead and other indirect expenses constituted a change of accounting method under section 481 of the Internal Revenue Code of 1954 in the taxable year 1965, and accordingly increased taxpayer's taxable income by $7,042,325.93.

Taxpayer filed a petition in the Tax Court on June 12, 1969, seeking a redetermination of these asserted deficiencies. Trial was held and the Tax Court sustained the assessed deficiencies. Taxpayer appeals from that decision.

Relying upon the doctrine of collateral estoppel, taxpayer first contends the Tax Court erred in ruling on the overhead capitalization issue because it was raised in the prior litigation. The doctrine of collateral estoppel is strictly applied in tax cases. *See, e.g.*, Trapp v. United States, 177 F.2d 1 (10th Cir. 1949), *cert, den'd,* 339 U.S. 913 (1950). It " '. . . is applicable only where an issue identical to that presented in the second case has been raised and fully adjudicated under identical and inseparable relevant facts in a prior action between the same parties involving a different tax year." Jones v. United States, 466 F.2d 131, 133 (10th Cir. 1972), *cert. den'd,* 409 U.S. 1125 (1973). *See also* CIR v. Sunnen, 333 U.S. 591 (1948), 1B Moore's Federal Practice ¶ 0.443[1] (2nd ed. 1974).

The overhead capitalization issue was, as taxpayer correctly contends, raised in the first case. However, no findings, either mediate or ultimate, were made with respect thereto, and there was no judicial determination of the issue. To obtain the protection afforded by the doctrine of collateral estoppel an issue must have been raised, litigated and actually

adjudged on the merits in the first proceeding.[1] Here, the overhead issue was raised but, because it was abandoned by the IRS, was not judicially determined. Under these circumstances collateral estoppel cannot apply.

Taxpayer nonetheless argues that conclusive effect should be given to the issue because it was raised and, although subsequently abandoned unilaterally, could therefore have been determined. We cannot agree. "In all cases . . . where it is sought to apply the estoppel of a judgment rendered upon one cause of action to matters arising in a suit upon a different cause of action, the inquiry must always be as to the point or question actually litigated and determined in the original action, not what might have been thus litigated and determined." United States v. International Bldg. Co., 345 U.S. 502, 505 (1952).[2]

It is next contended that the Tax Court erred in quashing taxpayer's subpoena duces tecum, which directed the IRS to produce "[a]ll reports, data and correspondence (including correspondence between Denver I.R.S. and the National office of I.R.S.) relating to respondent's abandonment of the accounting issues. . . . " We disagree. The IRS argued, at the hearing on its motion to quash the subpoena, that the requested information was privileged and irrelevant. Taxpayer responded by admitting that possibility, and thereafter failed to show a relevant purpose for the information. Based upon these facts we must conclude that the Tax Court properly quashed the subpoena duces tecum. Taxpayer now asserts that the purpose of the subpoena was "to expose the Com-

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[1]*See, e.g.*, CIR v. Sunnen, 333 U.S. 591 (1948); 1B Moore's Federal Practice ¶ 0.422[2] and 0.443[1] (2nd ed. 1974). *See also* Restatement, Judgments § 68(2) (1942), which provides: "A judgment on one cause of action is not conclusive in a subsequent action as to questions of fact not actually litigated and determined in the first action."

[2]*See also* 1B Moore's Federal Practice ¶ 0.443[4] (2nd ed. 1974): "The requirement that an issue must have been determined by adjudication in the prior action is also significant . . . in situations in which the issue was undoubtedly raised and litigated in the prior action, but . . . was not in fact determined. . . ."

missioner's ploy to circumvent the rule of collateral estoppel." That argument, however, was not raised below and will not be considered for the first time on appeal.

Taxpayer next asserts that the Tax Court erred in approving the IRS's change in its method of accounting. We do not believe the method of accounting used by taxpayer "clearly reflects income" as required by 26 U.S.C. § 446.[3] As stated earlier, taxpayer deducts, as operating expenses, the indirect costs of constructing its capital assets. The effect of this accounting procedure is twofold. The deduction of such costs and their concomitant omission from capital assets will understate the cost basis of said assets and will cause the cost of goods sold in a given year to be overstated. This will have the result of understating, and thus improperly reflecting, that year's income. And, any distortion in the cost basis of capital assets, normally recoverable through depreciation, will affect income in future years.

Moreover, the deduction of these costs is expressly prohibited by the Internal Revenue Code. Title 26 U.S.C. § 263(a) provides that "[n]o deduction shall be allowed for — (1) any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate." This includes the costs of self-construction and construction related expense items. *See* CIR v. Idaho Power Co., 418 U.S. 1 (1974), 26 C.F.R. § 1.263 (a)-2 (1974).

Having determined that taxpayer's method of accounting did not clearly reflect income, the IRS took appropriate measures, under the authority of 26 U.S.C. § 446(b), to conform taxpayer's method of accounting to the requirements of 26 U.S.C. § 263(a). This necessitated various adjustments

[3]26 U.S.C. § 446(b) provides: "If no method of accounting has been regularly used by the taxpayer, or if the method used does not clearly reflect income, the computation of taxable income shall be made under such method as, in the opinion of the Secretary or his delegate, does clearly reflect income."

pursuant to 26 U.S.C. § 481. That statue provides, inter alia, that where taxable income for any taxable year is computed under a method of accounting different from that utilized to compute taxable income for a preceding taxable year then "there shall be taken into account those adjustments which are determined to be necessary solely by reason of the change in order to prevent amounts from being duplicated or omitted, except there shall not be taken into account any adjustment in respect of any taxable year to which this section does not apply unless the adjustment is attributable to a change in the method of accounting initiated by the taxpayer." And, 26 C.F.R. § 1.481-1(a)(1) (1975) amplifies the meaning of a change in method of accounting to include a change in the overall method of accounting for gross income or deductions, or a change in the treatment of item. *See also* 26 C.F.R. § 1.446-1(e)(2)(ii)(a) (1975).

Taxpayer contends that such determination, computations and adjustments made by the IRS in this regard are both speculative and clearly erroneous. It makes numerous allegations of error but has failed to support any of these arguments with specific facts or legal authority. Our examination of the record discloses no clear error. Accordingly, we must affirm.

AFFIRMED.

APPENDIX F

JULY TERM, — AUGUST 25, 1975

Before The Honorable David T. Lewis, Chief Judge, The Honorable Delmas C. Hill, The Honorable Oliver Seth, The Honorable William J. Holloway, Jr., The Honorable Robert H. McWilliams, The Honorable James E. Barrett and The Honorable William E. Doyle, Circuit Judges.

ADOLPH COORS COMPANY,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

No. 74-1468

This matter comes on for consideration of the petition for rehearing and suggestion for rehearing en banc filed by the petitioner in the captioned cause.

Upon consideration whereof, the petition for rehearing is denied by Circuit Judges Hill, Seth and Barrett to whom the case was argued and submitted.

The petition for rehearing having been denied by the original panel to whom the case was argued and submitted and no member of the panel nor judge in regular active service on the Court having requested that the Court be polled on rehearing en banc, Rule 35, Federal Rules of Appellate Procedure, the suggestion for rehearing en banc is denied.

A true copy
Teste
Howard K. Phillips
Clerk, U. S. Court of
Appeals, Tenth Circuit

By MARY A. SHERMAN
Deputy Clerk

HOWARD K. PHILLIPS
HOWARD K. PHILLIPS, Clerk

APPENDIX G

Internal Revenue Code (1954)

"Sec. 6214. Determinations by Tax Court.

(a) Jurisdiction as to Increase of Deficiency, Additional Amounts, or Additions to the Tax. — The Tax Court shall have jurisdiction to redetermine the correct amount of the deficiency even if the amount so redetermined is greater than the amount of the deficiency, notice of which has been mailed to the taxpayer, and to determine whether any additional amount, or addition to the tax should be assessed, if claim therefor is asserted by the Secretary or his delegate at or before the hearing or a rehearing."

APPENDIX H

RULES OF PRACTICE AND PROCEDURE
UNITED STATES TAX COURT

Rule 123. Default and Dismissal.

(d) Effect of Decision on Default or Dismissal. A decision rendered upon a default or in consequence of a dismissal, other than a dismissal for lack of jurisdiction, shall operate as an adjudication on the merits.

Supreme Court, U. S.
FILED
JAN 15 1976
MICHAEL RODAK, JR., CLERK

No. 75-706

In the Supreme Court of the United States

OCTOBER TERM, 1975

ADOLPH COORS COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

ROBERT H. BORK,
Solicitor General,
Department of Justice,
Washington, D.C. 20530.

In the Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-706

ADOLPH COORS COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioner challenges the decision below which held that it was not entitled to a current deduction for its indirect or overhead construction costs.

1. Petitioner produces and sells beer. It uses its own employees and equipment to erect buildings and other improvements and additions to its plant and facilities. During 1965 and 1966, petitioner respectively employed 398 and 580 persons engaged in construction. However, for accounting and tax purposes, petitioner has never separately identified its construction department. It employs a system of accounting which results in the current deduction rather than capitalization of all indirect or overhead costs of the construction activities (Pet. App. E 116a).

In a prior Tax Court proceeding dealing with petitioner's tax liability for 1962 through 1964, the Commissioner

raised several issues, including the deductibility of petitioner's construction costs. Following a trial of all issues, the Commissioner abandoned his challenge to petitioner's deduction of its construction costs for the prior years then in issue. However, the Commissioner expressly stated in his brief in the Tax Court (Commissioner's Brief, Docket Nos. 3179-66, 3180-66, 3181-66, pp. 3-3a) that he was not conceding the correctness of petitioner's accounting treatment of the construction costs. See Pet. App. E 117a. Accordingly, the Tax Court noted in its opinion in that prior case that "[t]he Commissioner in his brief abandons the disallowances of deductions made in the deficiency notice * * * representing corporation costs of construction overhead and maintenance and costs of engineering department overhead" (Pet. App. E 117a).

In this case, which involves the years 1965 and 1966, the Commissioner again disallowed various deductions for costs of construction overhead. On the merits, the Tax Court upheld the Commissioner's determination that such costs must be capitalized and were nondeductible. In so holding, the Tax Court rejected petitioner's claim that the capitalization issue was barred by collateral estoppel (Pet. App. D 44a-114a). The court of appeals affirmed (Pet. App. E 115a-121a).

2. The court of appeals properly held that the prior Tax Court decision did not constitute an adjudication of the merits of the accounting treatment issue. In that earlier case, the Commissioner merely withdrew the issue from consideration of the Tax Court. Accordingly, the Tax Court made no findings regarding the capitalization matter and did not address itself in any manner to a resolution of the legal issue.

Petitioner's position is that the issue was "litigated" in the prior case because evidence was adduced at trial, and because the Tax Court decision determined tax liability without capitalizing the costs in question. The

central inquiry, however, is not whether there has been a merely formal determination of liability in an earlier proceeding, but whether there has been an adjudication of a controverted issue submitted under adversary circumstances. Indeed, this Court has rejected the application of collateral estoppel even where the earlier determination *may* have been on the merits, in the absence of an affirmative showing that it was in fact based on the merits. *United States* v. *International Building Co.*, 345 U.S. 502, 506.[1] Here, of course, it is undisputed that the merits of the capitalization issue were not adjudicated in the case involving the earlier tax years.

3. This Court has narrowly limited the role of collateral estoppel in tax cases, for reasons amply illustrated by this case. Petitioner's position, if adopted, "would serve an unjust cause: it would become a device by which a decision not shown to be on the merits would forever foreclose inquiry into the merits." *United States* v. *International Building Co., supra,* 345 U.S. at 506. Moreover, on the merits *Commissioner* v. *Idaho Power Co.,* 418 U.S. 1, holding that the costs of equipment used by the taxpayer to build its own facilities must be capitalized as part of the cost of the capital improvements, would foreclose petitioner's claim to a deduction.[2]

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[1]Accord: *Trapp* v. *United States,* 177 F.2d 1(C.A. 10), certiorari denied, 339 U.S. 913 (earlier decision based on agreement of the parties, and deficiency calculated according to the contentions of the taxpayer); *Hartford-Empire Co.* v. *Commissioner,* 137 F.2d 540, 542 (C.A. 2) (estoppel not applicable "to matters not actually litigated"); *Licavoli* v. *Nixon,* 312 F.2d 200, 202 (C.A. 6) (estoppel denied where prior decision was based on "a procedural technicality"); 1B Moore's *Federal Practice,* para. 0.443[3] (2d ed., 1974).

[2]In *Idaho Power Co.* the Court cited the Tax Court's decision in this case with approval. See 418 U.S. at 14.

4. There is an additional ground, which the court of appeals did not find necessary to discuss, which renders collateral estoppel inapplicable here.

The Court's decision in *Commissioner* v. *Idaho Power Co., supra,* represents an intervening change in the "legal atmosphere" which would vitiate the force of collateral estoppel. See *Commissioner* v. *Sunnen, supra,* 333 U.S. at 600. Since *Idaho Power* represented "a modification or growth in legal principles" applicable to the issue, it nullified any potential or purported collateral estoppel effect of the earlier Tax Court decision. *Commissioner* v. *Sunnen, supra,* 333 U.S. at 599-600.

For the reasons stated, it is respectfully submitted that the petition for a writ of certiorari should be denied.

ROBERT H. BORK,
Solicitor General.
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